

# PSAB/Asset Management

NEWSLETTER NO. 49

## LEGISLATED BUDGET REQUIREMENTS - THE BALANCING ACT

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The [Ontario Municipal Act](#) requires every Ontario municipality to prepare and approve a budget each year. For local municipalities the relevant provisions of the [Municipal Act](#) are found in [section 290](#). Similar requirements exist for upper tier municipalities in [section 289](#).

These sections spell out the so-called “balanced budget” requirement that is a prime directive for all Ontario municipalities. In short, a municipality must identify the source(s) of financing for all known financial obligations and disbursements, contracted and planned, that will come due in the fiscal year(s) covered by the budget. This requirement applies to the current operations of a municipality, as opposed to the capital operations of a municipality, which are addressed in a later section, which restricts the use of long-term debt financing to capital works purposes. The property tax levy and debenturing requirements are only two components of the complex annual financing equation.

Other sections of the Act empower municipalities to:

- (a) establish reserves and reserve funds for financing future anticipated needs (Section 293);
- (b) authorize temporary borrowing, to address short-term cash flow problems (Section 407);
- and
- (c) issue debentures for funding the acquisition of capital works (Section 401).

There has been considerable speculation over the past few years as to what would happen with the move to full accrual accounting and accounting for tangible capital assets, especially the impact on municipal budgets. The Ontario Municipal Act requires Ontario municipalities to issue audited financial statements annually (Section 294). To have an unqualified audit opinion on such statements, they would have to be prepared in accordance with the guidelines and recommendations of the Public Sector Accounting Handbook. Thus the accounting change will have a pronounced impact on the financial reporting, and we will look at this in detail in the next series of newsletters.

This also includes some major changes to the updated Ontario Financial Information Return that the Ministry of Municipal Affairs and Housing is implementing, starting with the 2009 Return. But what will be the impact on budgeting?

**Bill 162 (2009)**

The rules have changed somewhat, though the game is much the same. The 2009 Provincial Budget (Bill 162) included Schedule 19, which outlines ten changes to the Municipal Act. This Bill received Royal Assent on June 5, 2009, so is now in force.

In terms of budgeting and financing, Schedule 19 provides a way to get back to the same tax calculation. There is still the balanced budget requirement. Each municipality must still identify the source(s) of financing for all known financial obligations and disbursements, contracted and planned, that will come due in the fiscal year(s) covered by the budget. Municipalities are still no less empowered to establish reserves and reserve funds for financing future anticipated needs, to authorize temporary borrowing, to address short-term cash flow problems, and to issue debentures for funding the acquisition of capital assets. And you are still required to factor last year’s operations’ “surplus” or “deficit” into this year’s budget.

Thus the new legislation would seem to be almost a replay of the current legislation.

Let us now look at the changes:

<b>MUNICIPAL ACT (2001) BEFORE AMENDMENTS</b>	<b>BILL 162 (2009) SCHEDULE 19 - AMENDMENTS TO 2001 ACT</b>
	<p><b>1. Subsections 289 (2) to (6) of the Municipal Act, 2001 are repealed and the following substituted:</b> (budgets of upper tier municipality – not included here as they are similar to local municipality)</p>
<p><b>Yearly budget, local municipalities</b></p> <p><b>290.</b> (1) For each year, a local municipality shall, in the year or the immediately preceding year, prepare and adopt a budget including estimates of all sums required during the year for the purposes of the municipality, including,</p> <ul style="list-style-type: none"> <li>(a) amounts sufficient to pay all debts of the municipality falling due within the year;</li> <li>(b) amounts required to be raised for sinking funds or retirement funds; and</li> <li>(c) amounts required for any board, commission or other body. 2001, c. 25, s. 290 (1); 2006, c. 32, Sched. A, s. 120 (1).</li> </ul> <p><b>Exception</b></p> <p>(1.1) Despite subsection (1), a budget for a year immediately following a year in which a regular election is held, may only be adopted in the year to which the budget applies. 2006, c. 32, Sched. A, s. 120 (2).</p>	<p><b>2. Subsections 290 (2) to (5) of the Act are repealed and the following substituted:</b> (local municipality)</p>

<b>MUNICIPAL ACT (2001) BEFORE AMENDMENTS</b>	<b>BILL 162 (2009) SCHEDULE 19 - AMENDMENTS TO 2001 ACT</b>
<p><b>Detail and form</b></p> <p>(2) The budget shall,</p> <p>(a) in such detail and form as the Minister may require, set out the estimated revenues, including the amount the municipality intends to raise on all the rateable property in the municipality by its general local municipality levy and on less than all the rateable property in the municipality by a special local municipality levy under section 312, and the estimated expenditures; and</p> <p>(b) provide that the estimated revenues are equal to the estimated expenditures. 2001, c. 25, s. 290 (2).</p>	<p><b>Detail and form</b></p> <p>(2) The budget shall, in such detail and form as the Minister may require, set out the following amounts:</p> <ol style="list-style-type: none"> <li>1. The estimated revenues, including the amount the municipality intends to raise on all the rateable property in the municipality by its general local municipality levy and the amount it intends to raise on less than all the rateable property in the municipality by a special local municipality levy under section 312.</li> <li>2. The estimated portion of the estimated revenues described in paragraph 1, if any, to be paid into the municipality's reserve, sinking and retirement funds.</li> <li>3. The estimated expenses, subject to any regulation made under clause 292 (2) (a).</li> <li>4. The estimated portion of the estimated expenses described in paragraph 3, if any, to be paid out of the municipality's reserve, sinking and retirement funds.</li> </ol>
	<p><b>Reserve fund adjustment</b></p> <p>(3) The total calculated under paragraph 1 shall be at least equal to the total calculated under paragraph 2:</p> <ol style="list-style-type: none"> <li>1. The amount described in paragraph 1 of subsection(2), added to the amount described in paragraph 4 of subsection (2).</li> <li>2. The amount described in paragraph 2 of subsection(2), added to the amount described in paragraph 3of subsection (2).</li> </ol>
<p><b>Allowance</b></p> <p>(3) In preparing the budget for a year, the local municipality,</p> <p>(a) shall treat any operating surplus of any previous year as revenue that will be available during the year;</p> <p>(b) shall provide for any operating deficit of any previous year and for the cost of the collection of taxes and any abatement or discount of taxes;</p> <p>(c) shall provide for taxes and other revenues that in the opinion of the treasurer are uncollectible and for which provision has not been previously made;</p>	<p><b>Allowance</b></p> <p>(4) In preparing the budget for a year, the local municipality,</p> <p>(a) shall not include in the estimated revenues described in paragraph 1 of subsection (2) the estimated proceeds of any borrowing during the year;</p> <p>(b) shall treat as estimated revenues any surplus of any previous year that resulted because,</p> <ol style="list-style-type: none"> <li>(i) revenues for that year were greater than the amount described in paragraph 1 of subsection (2) for that year, or</li> </ol>

<b>MUNICIPAL ACT (2001) BEFORE AMENDMENTS</b>	<b>BILL 162 (2009) SCHEDULE 19 - AMENDMENTS TO 2001 ACT</b>
<p>(d) may provide for taxes and other revenues that it is estimated will not be collected during the year; and</p> <p>(e) may provide for such reserves as the municipality considers necessary. 2001, c. 25, s. 290 (3); 2006, c. 32, Sched. A, s. 120 (3).</p>	<p>(ii) expenses for that year were less than the amount described in paragraph 3 of subsection (2) for that year;</p> <p>(c) shall provide for any deficit of any previous year that resulted because,</p> <p>(i) revenues for that year were less than the amount calculated by deducting for that year the amount described in paragraph 2 of subsection (2) from the amount described in paragraph 1 of subsection (2), or</p> <p>(ii) expenses were incurred by the municipality that were not in the budget for that year and were not paid for that year from a reserve, sinking or retirement fund;</p> <p>(d) shall provide for the cost of the collection of taxes and any abatement or discount of taxes;</p> <p>(e) shall provide for taxes and other revenues that in the opinion of the treasurer are uncollectible and for which provision has not been previously made;</p> <p>(f) may provide for taxes and other revenues that it is estimated will not be collected during the year; and</p> <p>(g) may provide for such reserve funds as the municipality considers necessary.</p>
	<p><b>Exception, 2009</b></p> <p>(5) In preparing the budget for 2009, the local municipality,</p> <p>(a) shall treat any operating surplus of any previous year as estimated revenues for the purpose of paragraph 1 of subsection (2); and</p> <p>(b) despite clause (4) (c), shall provide for any operating deficit of any previous year.</p>
<p><b>Yearly budget from boards, etc.</b></p> <p>(4) Despite any other Act, for the purpose of preparing and adopting its budget for a year, the local municipality may by by-law require that the year's budget of every board, commission or other body, other than an upper-tier municipality or school board, for which the municipality is required by law to levy a tax or provide money, be submitted</p>	<p><b>Yearly budget from boards, etc.</b></p> <p>(6) Despite any other Act, for the purpose of preparing and adopting its budget for a year, the local municipality may by by-law require that the year's budget of every board, commission or other body, other than an upper-tier municipality or school board, for which the municipality is required by law to levy a tax or provide money, be submitted</p>

<b>MUNICIPAL ACT (2001) BEFORE AMENDMENTS</b>	<b>BILL 162 (2009) SCHEDULE 19 - AMENDMENTS TO 2001 ACT</b>
to the municipality on or before a date specified by the local municipality, and that the budget shall be in such detail and form as the by-law provides. 2006, c. 32, Sched. A, s. 120 (4).	to the municipality on or before a date specified by the local municipality and that the budget shall be in such detail and form as the by-law provides.
<p><b>Legislation Act, 2006</b></p> <p>(5) Part III (Regulations) of the <i>Legislation Act, 2006</i> does not apply to a requirement of the Minister under clause (2) (a). 2006, c. 21, Sched. F, s. 120 (7).</p>	<p><b>Legislation Act, 2006</b></p> <p>(8) Part III (Regulations) of the <i>Legislation Act, 2006</i> does not apply to a requirement of the Minister under subsection (2).</p>
	<p><b>Definition</b></p> <p>(9) In this section, “reserve fund” includes a reserve.</p>
<p>(4) For the second and each subsequent year to which a multi-year budget applies, the municipality shall, in the year or the immediately preceding year,</p> <p>(a) review the budget for that year;</p> <p>(b) make such changes as are required for the purpose of making the provisions of the budget for that year comply with the requirements of section 289, except clause 289 (3) (a) or section 290, except clause 290 (3) (a), as the case may be; and</p> <p>(c) readopt the budget for that year and for subsequent years to which the budget applies. 2006, c. 32, Sched. A, s. 121.</p>	<p><b>3. Clause 291 (4) (b) of the Act is repealed and the following substituted:</b></p> <p>(b) make such changes as are required for the purpose of making the provisions of the budget for that year comply with the requirements of section 289, except clause 289 (4) (b), or section 290, except clause 290 (4) (b), as the case may be; and</p>
<p><b>292.</b> (1) If changes in the financial reporting requirements of a municipality or local board affect the operating surplus or deficit of the municipality or local board, the Minister may make regulations,</p> <p>(a) phasing-in or authorizing the municipality or local board to phase-in the changes in its budget over a period of years; and</p> <p>(b) governing the phase-in. 2001, c. 25, s. 292 (1).</p> <p><b>Retroactive</b></p> <p>(2) A regulation under this section may be retroactive to January 1 of the year in which the regulation is made. 2001, c. 25, s. 292 (2).</p>	<p><b>4. Section 292 of the Act is repealed and the following substituted:</b></p> <p><b>Regulations, changes in financial reporting requirements</b></p> <p>292. (1) If changes in the financial reporting requirements of a municipality or local board affect the surplus or deficit of the municipality or local board, the Minister may make regulations,</p> <p>(a) phasing in or authorizing the municipality or local board to phase in the changes to its budgets over a period of years;</p> <p>(b) governing the phase-in.</p> <p><b>Regulations, budgets</b></p> <p>(2) The Minister may make regulations,</p>

<b>MUNICIPAL ACT (2001) BEFORE AMENDMENTS</b>	<b>BILL 162 (2009) SCHEDULE 19 - AMENDMENTS TO 2001 ACT</b>
	<p>(a) prescribing types of expenses that a municipality or local board may exclude from the estimated expenses described in paragraph 3 of subsection 289(2) and in paragraph 3 of subsection 290(2);</p> <p>(b) prescribing conditions that must be met before a municipality or local board may exclude from the estimated expenses the types of expenses pre-scribed under clause (a);</p> <p>(c) prescribing a date for the purposes of subsection(4).</p> <p><b>Retroactive</b>  (3) A regulation made under this section may be retro-active to January 1 of the year in which the regulation is made.</p> <p><b>Review</b>  (4) The Ministry of Municipal Affairs and Housing shall, on or before a prescribed date, initiate a review of any regulation made under clause (2) (a) or (b).</p>
<p>(10) If a local board is a local board of more than one municipality, only the auditor of the municipality which is responsible for the largest share of the operating costs of the local board is required to audit the local board. 2001, c. 25, s. 296 (10).</p>	<p><b>5. Subsection 296 (10) of the Act is repealed and the following substituted:</b></p> <p><b>Joint boards</b>  (10) If a local board is a local board of more than one municipality, only the auditor of the municipality that is responsible for the largest share of the expenses of the local board in the year is required to audit the local board in that year.</p>
<p><b>407.</b> (1) At any time during a fiscal year, a municipality may authorize temporary borrowing, until the taxes are collected and other revenues are received, of the amount council considers necessary to meet the current expenditures of the municipality for the year, including amounts required in the year for,</p> <ul style="list-style-type: none"> <li>(a) sinking and retirement funds;</li> <li>(b) principal and interest due on any debt of the municipality;</li> <li>(c) school purposes;</li> <li>(d) other purposes the municipality is required by law to provide for; and</li> <li>(e) the amount of principal and interest payable</li> </ul>	<p><b>6. (1) Subsection 407 (1) of the Act is amended by striking out the portion before clause (a) and clause(a) and substituting the following:</b></p> <p><b>Borrowing for expenses</b>  (1) At any time during a fiscal year, a municipality may authorize temporary borrowing, until the taxes are collected and other revenues are received, of the amounts that the municipality considers necessary to meet the expenses of the municipality for the year and of the amounts, whether or not they are expenses for the year that the municipality requires in the year for,</p>

<b>MUNICIPAL ACT (2001) BEFORE AMENDMENTS</b>	<b>BILL 162 (2009) SCHEDULE 19 - AMENDMENTS TO 2001 ACT</b>
<p>by a person or municipality primarily liable for a debt, if the municipality has guaranteed the debt and the debt is in default. 2001, c. 25, s. 407 (1).</p>	<p>(a) reserve, sinking and retirement funds;</p>
<p>(4) In subsections (2) and (3), estimated revenues do not include revenues derivable or derived from,</p> <ul style="list-style-type: none"> <li>(a) any borrowing, including through any issue of debentures;</li> <li>(b) a surplus, including arrears of taxes, fees or charges; or</li> <li>(c) a transfer from the capital fund, reserve funds or reserves. 2001, c. 25, s. 407 (4).</li> </ul>	<p><b>(2) Subsection 407 (4) of the Act is repealed and the following substituted:</b></p> <p><b>Exclusion</b>  (4) In subsections (2) and (3), estimated revenues do not include revenues derivable or derived from,</p> <ul style="list-style-type: none"> <li>a) arrears of taxes, fees or charges; or</li> <li>b) a payment from a reserve fund of the municipality, whether or not the payment is for a capital purpose.</li> </ul>
	<p><b>(3) Section 407 of the Act is amended by adding the following subsection:</b></p> <p><b>Definition</b>  (6) In this section, “reserve fund” includes a reserve.</p>
<p>(2) Subject to this Act and the regulations, a municipality may pass by-laws authorizing, with respect to its debentures or any class of them,</p> <ul style="list-style-type: none"> <li>(a) the due dates, amounts of and methods for payment of principal and interest, including electronic transfer of payments;</li> <li>(b) the maturity dates;</li> <li>(c) the form of execution and use of the municipal seal;</li> <li>(d) a registry;</li> <li>(e) tenders and a process for tendering;</li> <li>(f) redemption;</li> <li>(g) refinancing;</li> <li>(h) cancellation, substitution, exchange and transfer of ownership;</li> <li>(i) the form of instrument;</li> <li>(j) notices or other communications to persons with an interest;</li> <li>(k) the use of electronic, magnetic or other media for records of or related to the debentures or for copies of them. 2001, c. 25, s. 408 (2).</li> </ul>	<p><b>7. (1) Section 408 of the Act is amended by adding the following subsection:</b></p> <p><b>Restriction</b>  (2.1) A municipality may issue a debenture or other financial instrument for long-term borrowing only to provide financing for a capital work.</p>



<b>MUNICIPAL ACT (2001) BEFORE AMENDMENTS</b>	<b>BILL 162 (2009) SCHEDULE 19 - AMENDMENTS TO 2001 ACT</b>
(3) The term of a debt of a municipality or any debenture or other financial instrument for long-term borrowing issued for it shall not extend beyond the lifetime of the undertaking for which the debt was incurred and shall not exceed 40 years. 2006, c. 32, Sched. A, s. 176.	<b>(2) Subsection 408 (3) of the Act is amended by striking out “undertaking” and substituting “capital work”.</b>
(5) Except as provided in this section, no amount raised for a sinking or retirement fund, including earnings or proceeds derived from the investment of those funds, shall be applied towards paying any part of the current or other expenditure of a municipality. 2001, c. 25, s. 409 (5).	<b>8. (1) Subsection 409 (5) of the Act is repealed and the following substituted:</b>  <b>Limitation</b> (5) Except as provided in this section, a municipality shall apply an amount raised for a sinking or retirement fund, including earnings or proceeds derived from the investments of those funds, only towards repayment of the principal of the fund at maturity.
(12) If there is any amount remaining after applying the funds in accordance with subsection (11), the municipality may transfer the amount to the general fund of the municipality. 2001, c. 25, s. 409 (12).	<b>(2) Subsection 409 (12) of the Act is repealed and the following substituted:</b>  <b>Further amounts</b> (12) If there is any amount remaining after applying the funds in accordance with subsection (11), the municipality may use the amount for any purpose of the municipality.
<b>413.</b> (1) Subject to section 409 and this section, money received by a municipality from the sale of debentures, including any premium, and any earnings derived from the investment of that money, shall be applied only for the purposes for which the debentures were issued or for repayment of outstanding temporary borrowing under section 405 or 406 with respect to those debentures and shall not be applied towards payment of current or other expenditures of the municipality. 2001, c. 25, s. 413 (1).	<b>9. Subsection 413 (1) of the Act is repealed and the following substituted:</b>  <b>Use of money received</b> (1) Except as provided in section 409 and this section, money received by a municipality from the sale of debentures, including any premium, and any earnings derived from the investment of that money, shall be applied only for the purposes for which the debentures were issued or for repayment of outstanding temporary borrowing under section 405 or 406 with respect to those debentures.
<b>424.</b> (1) If a council applies any money raised for a special purpose or collected for a sinking or retirement fund to pay current or other expenditures otherwise than permitted by this Act, each member who votes for the application,  (a) is personally liable for the amount so applied which may be recovered in a court of competent jurisdiction; and	<b>10. Subsection 424 (1) of the Act is amended by striking out “to pay current or other expenditures” in the portion before clause (a).</b>



<b>MUNICIPAL ACT (2001) BEFORE AMENDMENTS</b>	<b>BILL 162 (2009) SCHEDULE 19 - AMENDMENTS TO 2001 ACT</b>
(b) is disqualified from holding any municipal office for two years. 2001, c. 25, s. 424 (1).	
	<p><b>Commencement</b></p> <p><b>11. (1) Subject to subsection (2), this Schedule comes into force on the day the Budget Measures Act, 2009 receives Royal Assent.</b></p> <p><b>(2) Sections 1 and 2 are deemed to have come into force on January 1, 2009.</b></p>

### **Budgeting and PSAB**

As we have noted several times in this series of newsletters on budgeting and PSAB, budgeting is not within the purview of the PSAB Handbook. A municipality may prepare and present a budget on any basis it wishes. The PSAB Handbook does require that budget numbers should be presented in the financial statements on the same basis and scope as the actuals shown. The actuals will be presented in accordance with PSAB standards, and the budget numbers will relate to the actuals. At the same time, the budget numbers reported in your financial statements must be reconcilable or relate back to the budget that was approved by Council. Your auditor will certainly require you to demonstrate this during the audit process. Your Council may require it too.

There is no requirement or compelling reason to change your current budget approach and process as a result of this accounting change, if you choose not to, at least for presentation to your Council.

### **Municipal Act, Section 292 (2)**

This paragraph empowers the Minister to issue regulations concerning municipal expenses that are not required to be financed in the fiscal year, and to prescribe conditions which must be met before excluding such expenses.

There is already a draft regulation, awaiting Ministerial approval and signature, that will be retroactive to January 2009, and which is to be reviewed before the end of 2012. A key term or provision of this Regulation is that a municipality may exclude from expenses, for the purposes of budgeting, all or a portion of:

- amortization expense;
- post-employment benefits; and
- landfill closure/post-closure expenses.

Others may be added to the list, over time. However, the caveat is that, beginning in 2010, the municipality shall, before adopting the budget, prepare a report with recommendations with respect to the excluded expenses, which is to be adopted by resolution of Council. This report is to include:

- an analysis of how the report's recommendations will impact on the accumulated surplus to the end of the year; and
- an analysis of the impacts of the report's recommendations on future funding requirements for tangible capital assets if the excluded expenses are not funded.

The good news is that you will not have to budget for amortization expense next year if your Council does not want you to. The bad news is that if you do not, you are going to have to present your Council with a detailed analysis of what the future financial impacts of that action will be, and that they are going to have to sign off that they agree with that approach, and that they know and understand the future implications of that course of action. And this is to be completed before you present your 2010 budget to your Council.

This may not be as bad as it seems. You may already make contributions to reserve and reserve funds from your Operating Fund to cover future major expenditures. Similarly, you may make capital expenditures from current funds, or have a capital levy. If you do, these amounts could be reallocated to take care of budgeting for items like amortization expense, so that no reporting would be required.

Note that the reporting is to your Council, and to your Council only, not to the Ministry. However, you must expect that while the Ministry will probably not be interested in the contents of your reporting, Ministry staff may well follow up to confirm for the record that your Council has indeed approved the required reporting.

Please go to <http://www.ontariocanada.com/registry/view.do?postingId=1785> for further details.

## Summary

The new legislative requirements with regard to budgeting do not impose new financial obligations on municipalities. You will continue to pay for operating expenses as they are incurred, and pay bond holders interest and repayment of principal when the amounts come due. New information with regard to assets has the potential to better inform your budget process, but does not necessarily require changes in the way you budget. However, the message is clear that if you do not budget for amortization expense or the consumption of TCAs, for example, your Council will have to sign off on their acceptance of the implications of doing so.

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From this discussion on budgeting and PS3150, you may well continue to have an operating budget and a capital expenditure program or a capital investment plan for each fiscal year. However, your accounting for capital assets will change from a fiscal year orientation to one reflecting the life cycle of the asset. You will account for the using up of tangible capital assets in your operating accounts, or the Revenue Fund, so what will be the future role of the "Capital Fund"? In short, does the implementation of PS3150 mean the end of fund accounting?

Our next newsletter will explore the case for and against the retention of fund accounting. This newsletter (#50) has actually already been published and posted on the PSAB website.

### **A Note on Reserves and Reserve Funds**

In addition to concern about how the balanced budget requirement may be legislated with respect to full accrual accounting and accounting for tangible capital assets, there have also been questions raised about the future use of reserves and reserve funds. We have been asked whether they will become illegal or irrelevant as a result of the change in accounting practices and financial reporting.

The logical answer might be “Only if your Council passes a bylaw to that effect.”

The setting up and use of reserves and reserve funds is a cash management tool and technique, to facilitate financing of intermittent, very variable or unknown costs. They are to be accounted for going forward, just as they are accounted for now, as part of net assets or accumulated surplus (or deficit). The revisions to the Municipal Act do not change the ability of municipalities to use reserves and reserve funds, and Public Sector Guideline 4 in the PSAB Handbook provides guidance on how they are to be reported, primarily as a schedule or note to the financial statements. We will come back to them in the future newsletters on financial reporting.

If they work for your municipality, continue to use them going forward.

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For more information and resources regarding tangible capital asset management, go to [PSAB/Asset Management](#) or contact:

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This Newsletter is published to assist you with your implementation of tangible capital asset accounting and with related matters. The Public Sector Accounting Handbook is the only authoritative primary source on matters relating to GAAP, and you should consult with your auditor to resolve specific issues that you may have.