

GASB Issues New Statement Related to Pollution Remediation

Statement Could Impact Public Sector Accounting and Liability Disclosures

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The Governmental Accounting Standards Board (GASB) has issued "Statement 49, Accounting and Financial Reporting for Pollution Remediation Obligations," which is intended to provide guidance for the accounting and reporting of obligations and costs related to pollution remediation. Redevelopment agencies should be aware of this new statement since it will impact the way agencies report liabilities on their financial statements.

The statement requires disclosure of liabilities associated with contaminated properties, including environmental assessment and cleanup, post-remediation monitoring, agency oversight fees, and legal expenses. It also addresses accounting and financial reporting standards for obligations to assess and remediate pollution.

Beginning December 15, 2007, the measurement of pollution remediation liabilities is required at the beginning of that period, so that beginning net assets can be restated. Further, if an agency presents multiple periods and has sufficient information to apply the expected cash flow technique to measurements in prior periods, then that agency would be required to apply the provision retroactively for all such prior periods presented.

There are five types of obligating events that will require an agency to report a remediation liability. Those types are as follows:

- ✧ An agency is compelled to take a remediation action because of an imminent danger to the public or environment. For example, a tanker truck spills gasoline on a road, and emergency responders are dispatched to clean up the release.
- ✧ An agency violates a pollution prevention-related permit or license. For example, many permits contain provisions that require the permittee to take certain actions in case of spills.
- ✧ An agency is named, or likely will be named, by a regulatory agency as a responsible or potentially responsible party for remediation or remediation costs. For example, a redevelopment agency acquires a property, discovers a release, and is then named the responsible party.

The scope of the statement does not include pollution prevention or control obligations, future asset retirement remediation activities, fines or penalties, toxic torts, or product and process safety outlays.

- ✧ An agency is named in a lawsuit, or likely will be named, to compel participation in remediation. For example, a property owner discovers petroleum contamination on his property and sues the government that owns an adjacent property and operates an underground storage tank.
- ✧ An agency commences or legally obligates itself to commence remediation. For example, in a DDA, a redevelopment agency might agree to conduct site remediation.

When an obligating event occurs, an agency will be required to estimate the components of the expected remediation outlays, and determine whether the outlays for those components should be accrued as a liability or capitalized when goods and services are acquired. This allows an agency to record liabilities on a component basis, as it becomes reasonably estimable. For example, when a release is discovered, it may not be reasonably estimable to state the cost of the entire cleanup. However, the cost of an additional assessment would be reasonably estimable and should be recorded as a liability.

Remediation outlays will usually not qualify for capitalization and would be accrued as a liability, as appropriate when a range of expected outlays is reasonably estimable. Liabilities would be estimated using the "expected cash flow" technique and reported in the financial statements. Under the expected cash flow technique, expected recoveries are also taken into account.

In addition to pollution remediation liability disclosures, the statement requires an agency to disclose: 1) the nature and source of the remediation obligation; 2) the methods and assumptions used to estimate liability; 3) the potential

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for changes in the estimate; and 4) a description of the remediation activities, or components, that are not yet reasonably estimable.

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The new statement has several possible significant ramifications for an agency. Complying with the statement will require additional staff hours and technical expertise, or funding to obtain the appropriate professionals. Agency personnel aware of the statement are most concerned about the unbudgeted staff time and funds that compliance with the statement will entail.

Further, most agencies depend on their bonding capacity for infrastructure and capital improvement funding. This is particularly true of financially strapped cities and redevelopment agencies that tend to be heavily impacted by brownfields. These cities and agencies are likely to have potentially large liabilities that may greatly limit their ability to borrow at reasonable rates, and therefore, leave them unable to maintain infrastructure or fund other services. In addition, the covenant agreements for existing bonds may contain liability limits. Conversely, if cities and agencies do not comply with the GASB statement, then they may not be able to cure audit results or may be able to secure only overly qualified audit results. Without proper audit results, governments may not be

able to borrow at market rates or worse yet, may be unable to issue debt at all.

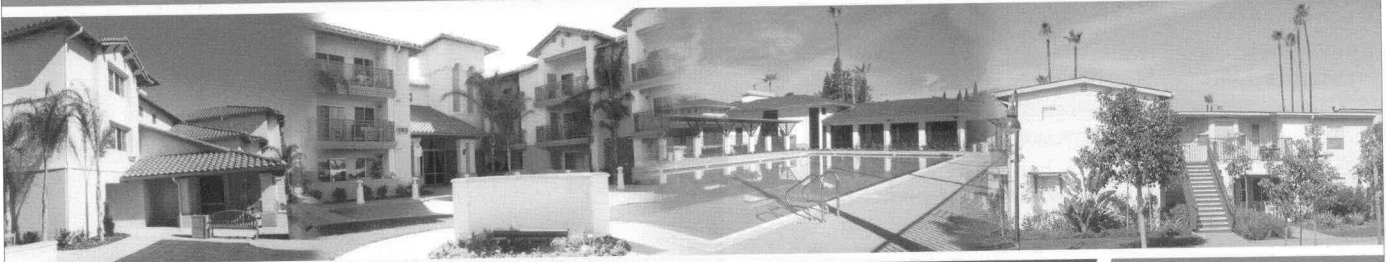
Once knowledge of Statement 49 becomes widespread, there may be a push by local governments including redevelopment agencies to get these liabilities off their books, either by cleaning up the impacted properties or transferring ownership to private interests.

While cities through their redevelopment agencies often acquire contaminated properties to facilitate redevelopment and frequently retain ownership of these properties for years, in the future, cities and agencies may avoid acquisition of contaminated properties to avoid liability. This might hinder redevelopment efforts, or it might be that a different model for redevelopment will evolve with developers taking on a more active role in acquisition and cleanup, and cities and agencies offering them additional tax breaks and other incentives to do so. Other strategies for controlling liability might involve environmental insurance policies to cap or offset liabilities, or increased use of risk transfer or liability buy out contracts and firms.

GASB Statement 49 could dramatically impact the way contaminated properties are financed by redevelopment agencies. In order to be prepared, redevelopment agencies must get involved *now*, assess the extent of their liabilities, and develop a plan of action.

For more information about GASB and the Statement 49 and/or download a copy of the Statement, visit the GASB website at www.gasb.org/project_pages/index.html.

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