State Accounting Office of Georgia
Fiscal Leadership for Georgia

Statewide Accounting Policy & Procedure

Accounting Manual Reference:	**Authoritative References:**	**Effective Date:** 06/30/2009
Section: Pollution Remediation Obligations	See Authority Section Below	**Revision Date:** 09/30/2009
Sub-section: N/A		

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Background and Scope:

The purpose of this policy is to prescribe statewide guidelines for complying with Governmental Accounting Standards Board (GASB) Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*. Statement No. 49 establishes uniform reporting standards for the financial reporting and disclosure requirements relating to pollution remediation obligations by governments. It defines when pollution remediation related obligations should be reported and how the costs and liabilities should be determined.

The scope of this policy, as required by Statement No. 49, covers remediation activities such as:

- Pre-cleanup activities including site assessment, feasibility study and design.
- Clean-up activities including neutralization, containment and disposal activities.
- Oversight and enforcement-related activities.
- Operation and maintenance of the remedy and monitoring.

Pollution prevention or control obligations relating to current operations and future pollution remediation activities that are required upon retirement of an asset, such as landfill closure and post closure care, are excluded.

Authority:

- GASB Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*
- GASB Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*
- SAO capital asset policies

Applicability:

Personnel with accounting and reporting responsibilities at all organizations included in the State of Georgia reporting entity should be knowledgeable of this policy.

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Policy:
Organizations included in the financial reporting structure of the State of Georgia are required to comply with the accounting provisions of Statement No. 49 beginning with the fiscal year ended June 30, 2009. In addition, these organizations are required to measure pollution remediation liabilities as of July 1, 2008 so that beginning net assets can be restated.

Accounting Requirements
Primary requirements of Statement No. 49:
Financial reporting and disclosure is required when a site operated by, or the responsibility of, any state organization is known to be polluted and one of five obligating events has occurred. Obligating events include the following:

1. The government is compelled to take pollution remediation action because of an imminent endangerment.
2. The government violates a pollution prevention–related permit or license.
3. The government is named, or evidence indicates that it will be named, by a regulator as a responsible party or potentially responsible party (PRP) for remediation, or as a government responsible for sharing costs.
4. The government is named, or evidence indicates that it will be named, in a lawsuit to compel participation in pollution remediation.
5. The government commences or legally obligates itself to commence pollution remediation.

Additional factors:
- The State is not required to search for additional potential remediation situations or expand its existing pollution remediation efforts, but simply to report a liability for all pollution remediation projects that meet one of the obligating events listed above.
- Obligations that can be reasonably estimated must be expensed, except under certain conditions where obligations can be capitalized (see capitalization requirements below).
- The liability must include direct expenses (for example payroll, materials, equipment, and legal and professional services) as well as indirect expenses (for example, general overhead).
- The amount to report is calculated based on an expected cash flow measurement technique.
- Obligations are reduced by recoveries, unless the recovery will result in a capital asset.

Capitalization Requirements: Pollution remediation outlays are to be capitalized when goods and services are acquired if acquired for any of the following four circumstances:

1. To prepare property in anticipation of a sale:
   Capitalize only amounts that would result in the carrying amount of the property not exceeding its estimated fair value upon completion of the remediation. Capitalization is appropriate only if the outlays take place within a reasonable period prior to the expected sale, or are delayed, but the delay is beyond the government's control.

2. To prepare property for use when the property was acquired with known or suspected pollution that was expected to be remediated:
   Capitalize only pollution remediation outlays necessary to place the asset into its intended location and condition for use. Capitalization is appropriate only if the outlays take place within a reasonable period following acquisition of the property, or are delayed, but the delay is beyond the government's control.

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3. To perform pollution remediation that restores a pollution-caused decline in service utility that was recognized as an asset impairment:
   Capitalize only pollution remediation outlays necessary to place the asset into its intended location and condition for use.

4. To acquire property, plant, and equipment that have a future alternative use:
   Capitalize outlays only to the extent of the estimated service utility that will exist after pollution remediation activities uses have ceased.

Classifications and Thresholds: State organizations must comply with the major asset classes described in SAO capital asset policies and the corresponding standard capitalization thresholds to account for and fully disclose capital asset activities under this policy. The SAO capital asset policies provide further details on major capital asset classes, such as:

- Definitions
- Depreciation methodology
- Capitalization thresholds
- Examples of expenditures (costs) to capitalize
- Examples of expenditures (costs) not to capitalize

Recognition and Measurement

If a government knows that a site is polluted and one or more of the obligating events has occurred, then it must attempt to estimate the current value of potential outlays for the cleanup. Under this standard, pollution remediation liabilities and expenses must be estimated using an "expected cash flows" measurement technique. This method essentially looks at the costs of potential cleanup actions and the probability of having to perform that action. The measurement involves assigning probabilities or likelihoods to each of the potential outlays and calculating a weighted average. Even though spending may occur over more than one year, Statement No. 49 does not require these cash flows to be discounted back to present value. The following example demonstrates the calculation.

> A government might estimate that there is a 10 percent chance that cleaning up a polluted site would cost $1 million, a 60 percent chance of $2 million, and a 30 percent chance of $3 million. The expected cash flow would be calculated as follows:
>
> ($1 million × 0.1) + ($2 million × 0.6) + ($3 million × 0.3) = $2.2 million.
>
> The $2.2 million would be reported as the liability in the government's financial statements.

If the outlay can be reasonably estimated, then the agency must report a liability in its full accrual financial statements under generally accepted accounting principles (GAAP). If the agency can estimate outlays for only certain portions of the cleanup effort—such as legal fees, testing the polluted site, or monitoring after the cleanup—then it must report a liability for those activities. The agency would then report liabilities for the remaining parts of the cleanup at a later time when ranges of outlays for them become reasonably estimable.

Recognition Benchmarks: These are steps in the remediation process that an agency is to consider in determining when components of pollution remediation liabilities are reasonably estimable:

- Receipt of an administrative order.
- Participation, as a responsible party or a PRP, in the site assessment or investigation.
- Completion of a corrective measures feasibility study.
- Issuance of an authorization to proceed.

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- Remediation design and implementation.

Expenses/Expenditures: Remediation outlays that are not eligible for capitalization treatment above must be reported as expenses (in proprietary and government-wide financial statements) or current expenditures (in governmental funds financial statements). These amounts must not be reported as part of an asset's value.

Expenses are reported by function/program in the government-wide Statement of Activities or as operating expenses, special items or extraordinary items in the proprietary funds Statement of Revenues, Expenses, and Changes in Fund Net Assets. Current expenditures are reported by function in the governmental funds Statement of Revenues, Expenditures, and Changes in Fund Balance.

Accounting for Estimated Recoveries: The following criteria relate to estimated recoveries –

- Recoveries that are not yet realized or not realizable reduce the expense and liability.
- Recoveries that are realized or realizable create an asset, reducing the expense to recognize but not the liability.
- Recoveries recognized after completion of remediation create an asset and revenue.
- Recoveries that are expected to result in capital assets will not reduce the remediation expense or liability. Those recoveries are to be recorded as revenue.

Basis of Accounting

Funds that operate on a statutory basis must convert their accounting activity to the modified accrual and/or accrual bases of accounting for the Comprehensive Annual Financial Report (CAFR). Proprietary and Fiduciary funds that do not operate on a statutory basis use the accrual basis of accounting throughout the year.

- Statutory Basis for Budgetary Compliance Reporting
  Activity is recorded as an expenditure on the statutory basis of accounting at the earlier of either the time the funds are encumbered (i.e., when purchase orders or other contractual obligations to procure goods or services have been executed) or the time the goods or services are received. Any accruals related to these expenditures are recorded as accounts payable or other short-term liabilities, not as pollution remediation obligations.

- Converting to Modified Accrual Basis for CAFR Reporting
  Encumbrance liabilities are eliminated under the modified accrual basis of accounting, and amounts that are expected to be liquidated with expendable available resources are recognized as liabilities when the goods and services are received. Pollution remediation liabilities do not represent an outflow of current available resources. Therefore, any accruals related to these expenditures are recorded as accounts payable or other short-term liabilities, not as pollution remediation obligations. Additionally, estimated recoveries of pollution remediation outlays from insurers or other responsible parties should reduce related expenditures when the recoveries are measureable and available.

- Converting to Accrual Basis for CAFR Reporting
  Current and noncurrent pollution remediation liabilities must be accrued for year-end government-wide reporting purposes. The current portion is for amounts payable within one year of the fiscal year-end. The noncurrent portion is for amounts payable in more than one year. The accruals should be reversed at the beginning of the next year.

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- Accrual Basis for Funds Not Reporting on a Statutory Basis
  Activity in these proprietary and fiduciary funds is reported throughout the year using the full accrual basis of accounting. Actual remediation expenses incurred during the year relieve the pollution remediation obligation. Current and noncurrent pollution remediation liabilities must be adjusted at each year-end. The current portion is for amounts payable within one year of the fiscal year-end. The noncurrent portion is for amounts payable in more than one year.

Disclosure Requirements
Footnote disclosures related to recognized pollution remediation liabilities are required and must include the following items:

- The nature and source of pollution remediation obligations (for example, federal, state or local laws or regulations),
- The amount of the estimated liability, the methods and assumptions used for the estimate, the potential for changes in the amount due to such items as price changes, new technology, or applicable laws or regulations, and
- Estimated amounts the State expects to recover from insurance or other parties since these amounts could reduce the liability.

In fiscal year 2009, the nature and effect of any restatement for pollution remediation obligations must be disclosed, including the adjustment to 2009 beginning balances. If the provisions of Statement No. 49 cannot be retroactively applied, the reason for not restating prior periods presented should be explained. If the liability cannot be reasonably estimated, then the agency must describe the nature of the pollution remediation in the notes to its financial statements.

As with other major classes of long-term liabilities, changes in the PRO liability should be presented in the notes to the financial statements, with governmental activities shown separately from business-type activities. A tabular format showing beginning balance, additions, deductions, ending balance, and amounts due within one year should be presented. Additionally, disclosure should be made of the governmental funds that typically are used to liquidate the PRO amounts.

General Accounting Procedures:
Identifying Transactions
To ensure compliance with the provisions of Statement No. 49, State of Georgia organizations must:

- Establish internal controls to ensure that obligating events are identified in a timely manner and that remediation liabilities are estimated correctly.
- Maintain an inventory of polluted sites for which they are responsible or potentially responsible.

Accounting Transactions and Journal Entries
No special journal entries for pollution remediation activities are required under the statutory or modified accrual bases of accounting. However, current and noncurrent liabilities must be recognized under the full accrual basis of accounting. Although no separate pollution remediation liability accounts are required by Statement No. 49, the SAO has established two separate accounts in the statewide financial system for this activity:

- 269000 Pollution Remediation – Current
- 279000 Pollution Remediation – Noncurrent

Organizations that do not use the statewide financial system must establish similar accounts. A comprehensive example of the entries required to convert from the statutory basis of accounting to other

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bases is provided in Attachment 1. An example of the entries required to account for recoveries is provided in Attachment 2.

Year-End Accounting Procedures

The SAO financial reporting group will request information about pollution remediation obligations as part of its year-end information package. Refer to the year-end form titled "Pollution Remediation (GASB49)." Organizations must provide the requested information to ensure that appropriate accrual basis adjusting entries are recorded for the annual financial reports. The threshold for reporting pollution remediation obligations is included in the *Materiality* policy. Each year the SAO financial reporting group will determine whether or not separate display of the pollution remediation liability is appropriate.

Definitions:

Current Value – The amount that would be paid if all equipment, facilities, and services included in the estimate were acquired during the current period.

Outlays – Expenses, expenditures, and capital acquisitions, as appropriate.

Pollution Remediation Obligation – An obligation to address the current or potential detrimental effects of existing pollution (e.g., hazardous wastes spills and asbestos contamination) by participating in pollution remediation activities such as site assessments and cleanups.

Potentially responsible party (PRP) – An individual or entity (including owners, operators, transporters, or generators) that is held potentially responsible for pollution at a site. As used in Statement No. 49, the term refers to a party that is held by law as potentially responsible for pollution at any site. It is not limited to parties associated with Superfund sites.

Pollution – The U.S. Environmental Protection Agency provides the following discussion of the term pollution on its website: "Generally, the presence of a substance in the environment that because of its chemical composition or quantity prevents the functioning of natural processes and produces undesirable environmental and health effects. Under the Clean Water Act, for example, the term has been defined as the man-made or man-induced alteration of the physical, biological, chemical, and radiological integrity of water and other media."

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Attachment 1

Pollution Remediation Obligation (PRO) Example – Conversion from Statutory Basis of Accounting to Other Bases

Assumptions:	Year 1	Year 2
• Purchase order for professional remediation services	1,500	
• Services received during the year	900	600
• Services processed by AP during the year	700	800
• PRO liability at beginning of year 1	(2,000)	
• PRO liability at end of year	(1,100)	(600)
• Current portion of PRO liability at end of year	(600)	(500)
• Estimated increase to PRO estimate at end of year 2 (No PO or AP)		(100)

Basis of Accounting	Journal Entry / Year-End Balance Descriptions	Governmental, Proprietary & Fiduciary Funds that Operate on a Statutory Basis		Proprietary & Fiduciary Funds that Operate Only on the Full Accrual Basis	
	Debit / (Credit)	Year 1	Year 2	Year 1	Year 2
Statutory Basis:					
Execute purchase order	Expenditure	1,500	-		
	Encumbrance Liability	(1,500)	-		
Process voucher through AP	Expenditure	700	800		
	Accounts Payable	(700)	(800)	N/A	N/A
Reduce Encumbrance	Encumbrance Liability	700	800		
	Expenditure	(700)	(800)		
At year-end accrue received/ not processed-reverse next year	Encumbrance Liability	200	(200)		
	Accounts Payable	(200)	200		
Year-end balances	Expenditure/Fund Balance	1,500	1,500		
	Accounts Payable	(900)	(1,500)		
	Encumbrance Liability	(600)	-		
Modified Accrual Basis: The change in the encumbrance liability is offset to expenditure:					
Reverse ending encumbrance	Encumbrance Liability	600	-		
	Expenditure	(600)	-	N/A	N/A
Adjust beginning fund balance for prior year encumbrance bal	Expenditure	-	600		
	Beginning Fund Balance	-	(600)		
Year-end balances	Expenditure/Fund Balance	900	1,500		
	Accounts Payable	(900)	(1,500)		
Full Accrual Basis:					
Full accrual only - Establish PRO liability at beginning of year 1	Net Assets			2,000	
	PRO - Noncurrent			(2,000)	
Conversion entry - Recognize PRO liability at year-end	Expense (change in total PRO liability)	(900)	(500)		
	Net Assets (PRO as of beg of year)	2,000	1,100		
	PRO - Noncurrent (PRO at end of year)	(1,100)	(600)		
Full accrual only - Payments processed against PRO liability	PRO - Noncurrent			900	600
	Accounts Payable			(900)	(600)
Full accrual only - Estimated increase to PRO at year-end	Expense				100
	PRO - Noncurrent				(100)
Reclassify current portion from noncurrent	PRO - Noncurrent	600	500	600	(100)
	PRO - Current	(600)	(500)	(600)	100
Year-end balances	Expense/Net Assets	2,000	2,100	2,000	2,100
	Accounts Payable	(900)	(1,500)	(900)	(1,500)
	PRO - Current	(600)	(500)	(600)	(500)
	PRO - Noncurrent	(500)	(100)	(500)	(100)

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Attachment 2

Example Journal Entries for Recording Recoveries

Assume that estimated remediation spending is $10,000 and expected insurance recoveries will be $3000.

To record the pollution remediation obligation if the expected recovery is not yet realizable:

Debit	$7000	Applicable Expense, Special Item or Extraordinary Item Accounts
Credit	$7000	Pollution Remediation – Current or Noncurrent

To record an increase to the pollution remediation obligation if the expected recovery is realized or becomes realizable at a later date, while remediation activities are still in progress:

Debit	$3000	Cash, Accounts Receivable or Other Non-capital Asset Account
Credit	$3000	Pollution Remediation – Current or Noncurrent

To record the pollution remediation obligation if the expected recovery is realized or realizable at the time of the initial estimate:

Debit	$7000	Applicable Expense, Special Item or Extraordinary Item Accounts
Debit	$3000	Cash, Accounts Receivable or Other Non-capital Asset Account
Credit	$10000	Pollution Remediation – Current or Noncurrent

To record the recovery if it is realized or becomes realizable after completion of remediation:

Debit	$3000	Cash, Accounts Receivable or Other Asset Account
Credit	$3000	Other Revenue

To record the obligation and recovery if the recovery will result in a capital asset:

Debit	$10000	Applicable Expense, Special Item or Extraordinary Item Accounts
Credit	$10000	Pollution Remediation – Current or Noncurrent

Debit	$3000	Capital Asset Account
Credit	$3000	Other Revenue

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