

SUMMARY OF STATEMENT NO. 49



SUMMARIES / STATUS

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ACCOUNTING AND FINANCIAL REPORTING FOR POLLUTION REMEDIATION OBLIGATIONS

(ISSUED 11/06)

This Statement addresses accounting and financial reporting standards for pollution (including contamination) remediation obligations, which are obligations to address the current or potential detrimental effects of *existing* pollution by participating in pollution remediation activities such as site assessments and cleanups. **The scope of the document excludes pollution prevention or control obligations with respect to current operations**, and future pollution remediation activities that are required upon retirement of an asset, such as landfill closure and post closure care and nuclear power plant decommissioning.

As illustrated in the flowchart in paragraph 106, once any one of five specified obligating events occurs, a government is required to estimate the components of expected pollution remediation outlays and determine whether outlays for those components should be accrued as a liability or, if appropriate, capitalized when goods and services are acquired. Obligating events include the following:

- The government is compelled to take pollution remediation action because of an imminent endangerment.
- The government violates 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 (PRP) 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 participation in pollution remediation.
- The government commences or legally obligates itself to commence pollution remediation.

Pollution remediation outlays should be capitalized in government-wide and proprietary fund financial statements, subject to certain limitations, only if the outlays are incurred (1) to prepare property for sale in anticipation of a sale, (2) to prepare property for use when the property was acquired with known or suspected pollution that was expected to be remediated, (3) to perform pollution remediation that restores a pollution-caused decline in service utility that was recognized as an asset impairment, or (4) to acquire property, plant, and equipment that have a future alternative use other than remediation efforts.

Most pollution remediation outlays do not qualify for capitalization and should be accrued as a liability (subject to modified accrual provisions in governmental funds) and expense when a range of expected outlays is reasonably estimable or as an expenditure upon receipt of goods and services. If a government cannot reasonably estimate the range of all components of the liability, it should recognize the liability as the range of each *component* (for example, legal services, site investigation, and required post remediation monitoring) becomes reasonably estimable. In government-wide and proprietary fund financial statements, the liability should be recorded at the current value of the costs the government expects to incur to perform the work. This amount should be estimated using the expected cash flow technique, which measures the liability as the sum of probability-weighted amounts in a range of possible estimated amounts—the estimated mean or average.

For pollution remediation obligations that are not common or similar to situations at other sites with which the government has experience, this Statement includes a series of recognition benchmarks—steps in the remediation process—that governments should consider in determining when components of pollution remediation liabilities are reasonably estimable. Thus, the measurable transactions and events that result in a pollution remediation liability may be relatively limited at initial recognition but would increase over time as more components become reasonably estimable. This Statement also requires remeasurement of the liability (and its components) when new information indicates increases or decreases in estimated outlays.

The measurement of a government's pollution remediation liability should include remediation work that the government expects to perform for other parties; however, expected recoveries from those other parties, and insurance recoveries, reduce the measurement of the government's pollution remediation expense when reasonably estimable (and reduce associated expenditures when the recoveries are measurable and available). If the expected recoveries are not yet realized or realizable, they also would reduce the measurement of the government's pollution remediation liability. If the expected recoveries are realized or realizable, they should be reported as recovery assets (for example, cash or receivables).

For recognized pollution remediation liabilities and recoveries, this Statement requires governments to disclose the nature and source of pollution remediation obligations, the amount of the estimated liability (if not apparent from the financial statements), the methods and assumptions used for the estimate, the potential for changes in estimates, and estimated recoveries that reduce the measurement of the liability. Governments are required to disclose a general description of the nature of pollution remediation activities for liabilities (or components thereof) that are not reasonably estimable.

The requirements of this Statement are effective for financial statements for periods beginning after December 15, 2007, with measurement of pollution remediation liabilities required at the beginning of that period so that beginning net assets can be restated. However, governments that have sufficient objective and verifiable information to apply the expected cash flow technique to measurements in prior periods are required to apply the provisions retroactively for all such prior periods presented.

How This Statement Will Improve Financial Reporting

This Statement will enhance comparability of financial statements among governments by requiring all governments to account for pollution remediation obligations in the same manner, including required reporting of pollution remediation obligations that previously may not have been reported. This Statement also will enhance users' ability to assess governments' obligations by requiring more timely and complete reporting of obligations as their components become reasonably estimable. Current standards (NCGA Statement 4, *Accounting and Financial Reporting Principles for Claims and Judgments and Compensated Absences*, and Financial Accounting Standards Board (FASB) Statement No. 5, *Accounting for Contingencies*) do not require recognition of pollution remediation

liabilities until after they are judged to be probable of occurrence. This causes a number of expected liabilities not to be reported. Additionally, current standards require the liability to be reported as a single-point estimate, which may not consider all potential outcomes. For example, FASB Interpretation No. 14, *Reasonable Estimation of the Amount of a Loss*, requires recognition of the low end of a range of estimated pollution remediation outlays when no amount within a range is a better estimate than any other amount. This causes reporting of liabilities at amounts that may differ significantly from the expected amounts (the amounts that, on average, will be incurred). This Statement will improve financial reporting by requiring consideration of recognition once an obligating event occurs and by requiring reporting of liabilities using the expected cash flow measurement technique.