
Betty Montgomery Auditor of State

Bulletin 2005-006

Date Issued: November 18, 2005

TO: County Auditors
City Finance Directors and Auditors
School District Treasurers
ESC Treasurers
Community School Finance Officers
Township Trustees and Clerks
Village Clerks, Clerk-Treasurers, and Finance Directors
Library Clerks, Treasurers, and Directors
Special Districts
County Family and Children First Councils
Law Libraries
Metropolitan Housing Authorities
Airport Authorities
Park Districts
Soil Water Conservation Districts
Water/Sewer Districts
Councils of Government
Cemeteries
Hospitals
Governmental Insurance Pools
Community Improvement Corporations
Development Corporations
Convention & Visitor Bureaus
Adult and Juvenile Correctional Facilities
County, City, Township Jails
Transit Authorities
Port Authorities
Fire and Ambulance Districts
Ohio Watershed Conservancy Districts
Agricultural Societies
Multi-County Health and MH/ADAS Boards
Colleges and Universities
College Foundations
Independent Public Accountants

FROM: Betty Montgomery
Auditor of State of Ohio

SUBJECT: GASB Statement No. 40 – Determining “Credit Ratings”

Overview

Pursuant to Statement No. 40 from the Government Accounting Standards Board (GASB), entitled *Deposit and Investment Risk Disclosures*, governments that prepare their financial statements in accordance with generally accepted accounting principles (GAAP) must disclose credit rating information related to their deposits and investments in the notes to their financial statements. This disclosure requirement also applies to those governments that prepare their financial statements in accordance with an other comprehensive basis of accounting (OCBOA); and therefore, their financial statements substantially conform with GAAP display requirements (see Auditor of State Bulletin 2005-002).

The Auditor of State's Office (AOS) has received inquiries as to how to obtain credit rating information. This Bulletin offers guidance on obtaining these ratings from nationally recognized statistical rating organizations. For most Ohio governments GASB Statement No. 40 becomes effective for fiscal years ending June 30, 2005 or December 31, 2005.

Disclosure Requirement

The following excerpt from GASB Statement No. 40 describes the responsibility of governments to provide credit rating information on their investments:

Governments should provide information about the credit risk associated with their investments by disclosing the credit quality ratings of investments in debt securities as described by nationally recognized statistical rating organizations—rating agencies—as of the date of their financial statements (for example, by aggregating the amount of investments by rating categories). Unless there is information to the contrary, obligations of the U.S. government or obligations explicitly guaranteed by the U.S. government are not considered to have credit risk and do not require disclosure of credit quality. Governments should disclose the credit quality ratings of external investment pools, money market funds, bond mutual funds, and other pooled investments of fixed-income securities in which they invest. If a credit quality disclosure is required and the investment is unrated, the disclosure should indicate that fact.

Credit Rating Organizations

To illustrate the process of obtaining the credit rating information, we will use three nationally recognized statistical rating organizations: Moody's, Standard & Poors, and Fitch. Each of these organizations can be accessed online at the following web addresses:

- Moody's: <http://www.moodys.com/cust/default.asp>
- Standard & Poors:
<http://www2.standardandpoors.com/servlet/Satellite?pagename=sp/Page/FixedIncomeFindRatingsPg&r=1&l=EN&b=2&s=142>

➤ Fitch: <http://www.fitchratings.com/corporate/products/fitchProducts.cfm?detail=2>

Note: Moody's and Standard & Poors both require you to register with them in order to use their sites, however, neither organization charges for the information provided.

Obtaining the Credit Rating

Let's take an example investment and walk through how to obtain its credit ratings. Let's assume that the government invested in GMAC (General Motors Acceptance Corporation) bonds.¹

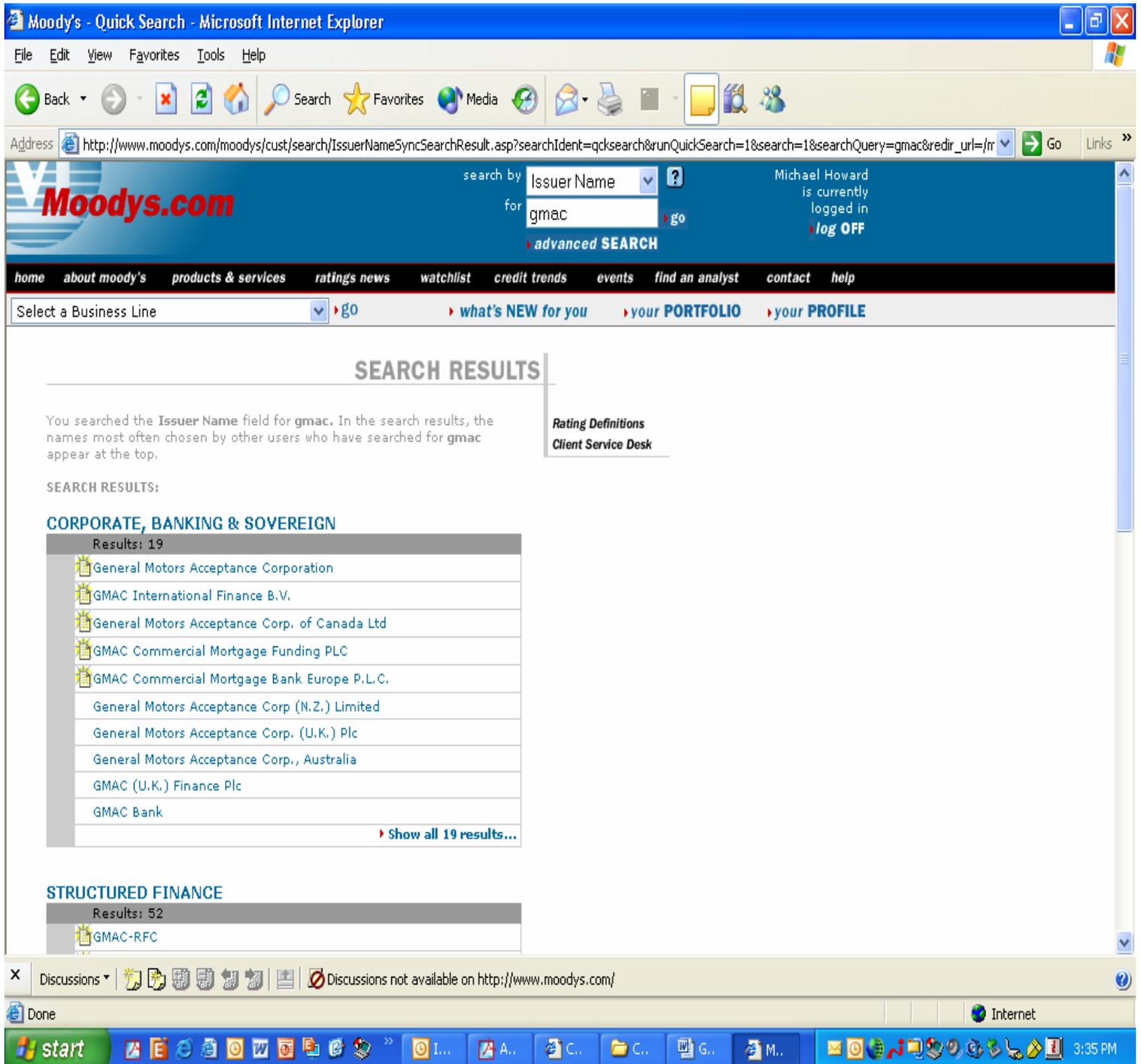
1. Go to the website indicated. We will use Moody's first for this example, but the process is similar for the other two organizations.
2. You will see the following screen:

¹ Such bonds may or may not be legal investments for any type of government. This investment vehicle was chosen for illustrative purposes only. Governments should consult the Ohio Revised Code and their own legal counsel regarding proper and legal investments.



3. In the upper right hand corner of the screen you will see a search box asking you how you want to search. The most exact way is by CUSIP number, a number assigned to most investments and easily obtainable from the confirmation statements you received when purchasing the investment. However, for this example, let's just enter "GMAC" as the descriptor and use the default "issuer name" box. Enter GMAC into the "for" box.

4. Once the search is performed, you will see the following screen:



5. Click on “General Motors Acceptance Corporation,” the first entry.

6. Once GMAC is selected and you scroll down to the detailed information, you will see the following screen:

Moody's - Quick Search - Microsoft Internet Explorer

File Edit View Favorites Tools Help

Address http://www.moody's.com/moodys/cust/qckSearch/qckSearch_search_result.asp?n_id=317000&fr_ref=C&PB2_nam=General+Motors+Acceptance+Corporation&searchQue Go Links >>

Issuer Details

Ticker: GM
Domicile: UNITED STATES
Previous Name:

Broad Industry: FINANCE
Specific Industry: FINANCE-CAPTIVE

Analyst Information

Analyst: Mark L. Wasden
Backup Analyst: Michael L. Mascarenhas
Managing Director: Robert Young
Rating Group: Financial Institutions
[Contact Moody's](#)

Rating Information

Long Term Rating: Baa2, Apr 5 2005 , LT Issuer Rating
ST Most Recent Rating: P-2, Jan 20 2004 , Other Short Term - Fgn Curr Rating(s) Under Review, 7 JUL 2005
Outlook:
Watchlist Status: Yes
Direction: See Detail
Date:

Current Rating List

200 of 1505 records

Debt Id	Class	Curr	Rating	Date	Action	Watch	Direction/Date
370424BK8	Senior Unsecured	USD	Baa2	5 APR 2005	Downgrade	Yes	Possible Downgrade 7 JUL 2005
370424CF8	Senior Unsecured	USD	Baa2	5 APR 2005	Downgrade	Yes	Possible Downgrade 7 JUL 2005
370424CZ4	Senior Unsecured	USD	Baa2	5 APR 2005	Downgrade	Yes	Possible Downgrade 7 JUL 2005
370424DA8	Senior Unsecured	USD	Baa2	5 APR 2005	Downgrade	Yes	Possible Downgrade 7 JUL 2005
	Senior Unsecured	USD	Baa2	5 APR 2005	Downgrade	Yes	Possible Downgrade 7 JUL 2005
370424DY6	Senior	USD	Baa2	5 APR 2005	Downgrade	Yes	Possible

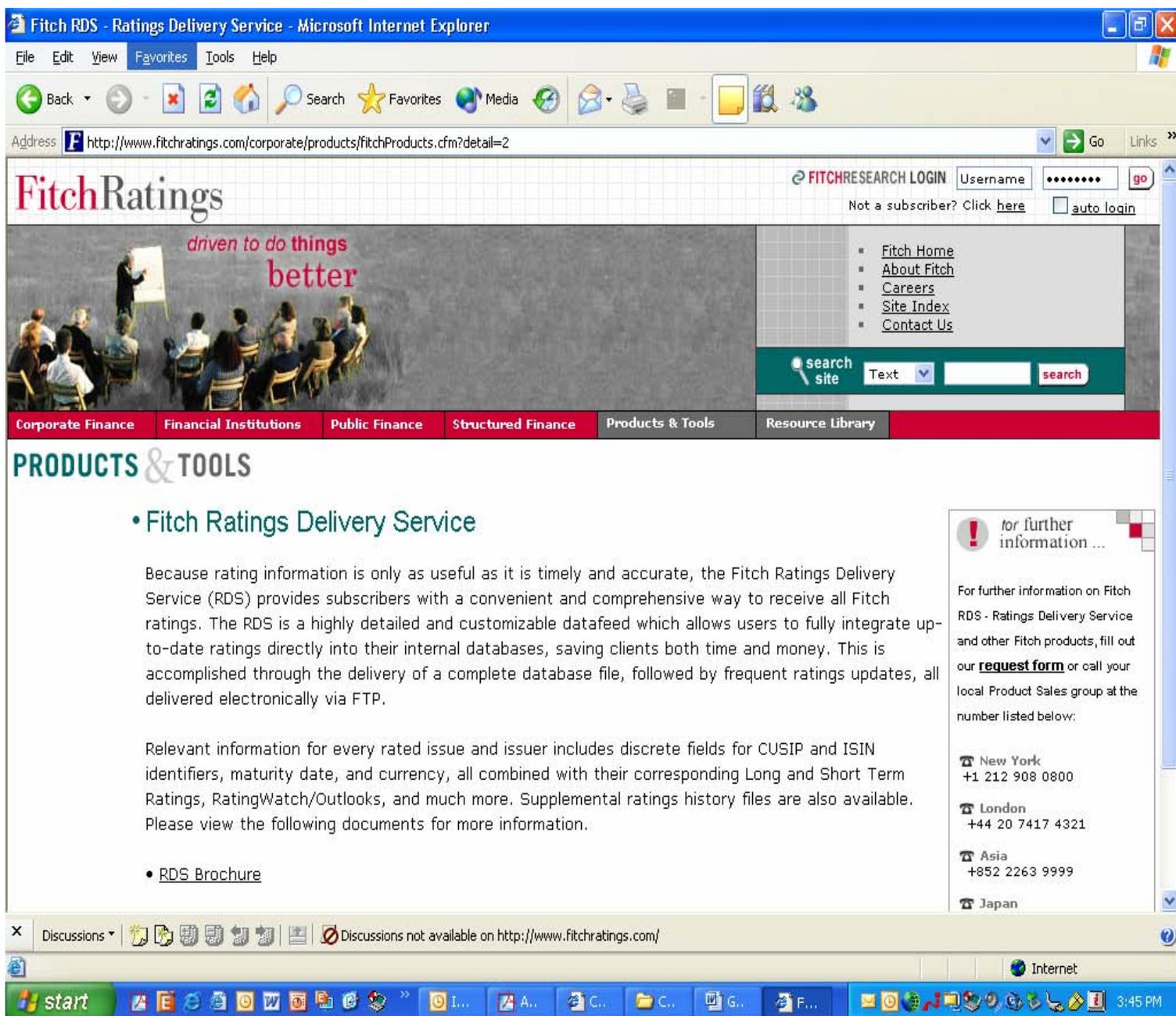
Discussions not available on <http://www.moody's.com/>

Done Internet

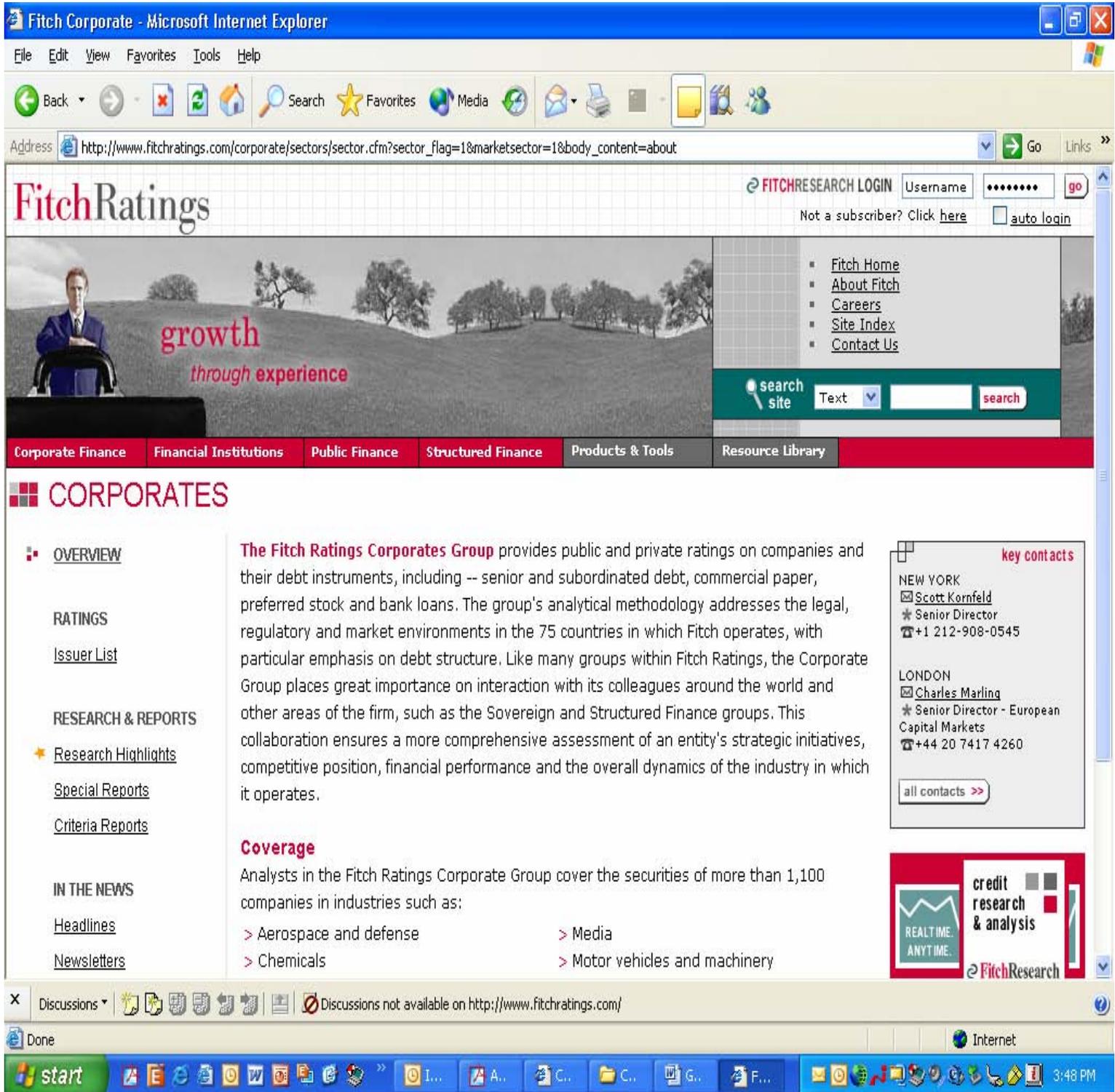
start I... A.. C.. G.. M.. 3:38 PM

- Identify your particular investment issue and determine its credit ratings. Note that in this example, the last ratings were April 5, 2005. Since this Bulletin was written in August 2005, and these screens were copied on August 17, 2005, these ratings are valid for governments which had such investments as of June 30, 2005. Note, however, that if the information was desired for December 31, 2004 for some reason, your government could not determine those ratings as of that date. Further, because this is a required disclosure under GASB Statement No. 40, your government might not be able to receive an “unqualified” opinion on your financial statements if the investments are material.

The following abbreviated steps may be used for those governments that wish to obtain the rating information through Fitch. GMAC will again be used as the example investment.



1. Click on "Corporate Finance" [first red button] or "Public Finance" [third red button] which will bring you to the ratings screens for corporate debt and government debt, respectively. After clicking "corporate finance," you will see the following screen:



2. Click on "Ratings," then, in this case, "G", then scroll to GMAC and eventually you will see the following screen:

Walker Jr., Philip S

Identifier(s): FIRST CALL TICKER: GM
 BLOOMBERG TICKER: GM
 FITCH TICKER: GM1
 CUSIP: 37040Z

Credit Ratings

Long Term Rating: BB+ 24-MAY-2005 Downgrade **Outlook: Negative**

Short Term Rating: B 24-MAY-2005 Downgrade

Rated Issues

	POSITIVE	NEGATIVE	EVOLVING	STABLE
OUTLOOK	+	-	↓	○
WATCH	▲	▼	◆	n/a

[show /hide all](#)

COMMERCIAL PAPER

Cp

SENIOR SHELF

Debentures

SENIOR UNSECURED

Bonds

MATURITY DATE	CURRENCY	TOTAL AMOUNT	COUPON RATE	RATINGS		CUSIP	ISIN
				LONG TERM	SHORT TERM		
15-JUN-2007	JPY	60,000,000,000	1.34%	BB+	--	--	JP584108A464
21-DEC-2007	JPY	33,000,000,000	1.29%	BB+	--	--	JP584108A3C1

Debentures

Medium-Term Notes

Using Standards & Poors, governments will follow virtually the same steps as with the other credit rating organizations.

The screenshot displays the Standard & Poor's website interface within a Microsoft Internet Explorer browser window. The browser's title bar reads "S&P Credit Ratings - Microsoft Internet Explorer". The address bar contains the URL: <http://www2.standardandpoors.com/servlet/Satellite?pagename=sp/Page/FixedIncomeFindRatingsPg&r=1&=EN&b=2&s=142>. The website header features the McGraw-Hill Companies logo and the Standard & Poor's logo. Navigation options include "Register! (Optional)", "Sign In", and a search box. A primary menu lists "Credit Ratings", "Indices", "Equity Research", "Risk Solutions", "CVC", "Funds", and "Data Services". A secondary menu includes "home", "products a-z", "our events", "about us", "press room", "contact us", and "careers". The left sidebar contains "Credit Ratings" and "Browse By Sector (GICS®)" with sub-categories such as Energy, Materials, Industrials, Consumer Discretionary, Consumer Staples, Health Care, Financials, Information Technology, Telecommunications Services, and Utilities. The main content area is titled "Find a Rating" and includes sections for "Credit Ratings Actions", "Credit Ratings Search", and a disclaimer about "Ratings Services". The right sidebar features "Credit Ratings Products & Services" and "More Credit Ratings Products & Services". The browser's taskbar at the bottom shows various application icons and the system clock at 3:54 PM.

1. Click on "Credit Ratings" \ "Find a Rating" and proceed in same manner as the other two sites to obtain the desired rating information.

Regardless of the credit rating organization used, governments should print the ratings and make them available to their financial statement preparers and auditors. Further, because the ratings change periodically, it is **critical** for governments to obtain these ratings for investments *at or as near as possible to fiscal year-end*.

Credit Ratings for Uninsured Issuances of Federal Agencies and Instrumentalities

Implementation Guide Q. 1.35 requires disclosing credit risk for the securities of Federal agencies and instrumentalities if the Federal Government does not guarantee them. Uninsured agencies include:

- The Federal Home Loan Mortgage Corporation (Freddie Mac)
- The Federal Home Loan Bank
- The Federal National Mortgage Corporation (Fannie Mae)
- Federal Farm Credit Banks

It is normally simpler to use the credit ratings from the sites below than to use the ratings from the previously described agency websites. The ratings described below are normally suitable evidence supporting credit risk disclosures. These sites cover the most common uninsured Federal agencies in which governments commonly invest:

http://www.freddiemac.com/investors/credit_reports.html

<http://www.fhlb-of.com/index.html> (click on FAQ, then see, “**What is the credit rating of the FHLBank System?**”)

http://www.fanniemae.com/markets/debt/understanding_fm_debt/debt_issuance_activities.jhtml?p=debt

www.farmcredit-ffcb.com/farmcredit/fcsystem/faqs.jsp

STAR Ohio

STAR Ohio discloses its rating in its annual report. The rating as of June 30, 2005 from Standard & Poor’s is AAAm.² You should check subsequent annual reports, but in the meantime we will notify you if this rating changes. See <http://www.treasurer.state.oh.us/star.htm> for the STAR Ohio annual report.

² The “m” in the rating stands for “municipal,” and is a credit modifier. The GASB Comprehensive Implementation Guide (Q. 1.33) does not require disclosing credit modifiers.

Additional Guidance from GASB

Oftentimes, investment securities have ratings from more than one rating organization, and sometimes those ratings differ. Further, it is possible that the various rating organizations will have different ratings on the same debt issuance. According to *GASB's Statement 40 Implementation Guide*, when multiple ratings exist, governments should, at a minimum, present the rating indicative of the greatest degree of risk. However, a government may also choose to disclose additional credit ratings, thereby presenting the user with additional credit risk information from which to ascertain the credit risk of the investment.

In many cases rating organizations provide split ratings for short-term and long-term investing; however, *GASB's Statement 40 Implementation Guide* does not specifically address which ratings to disclose when split ratings exist. In these cases the AOS recommends that governments disclose the ratings indicative of the greater degree of risk, similar to GASB's guidance on multiple ratings.

Furthermore, it is important for readers of the financial statements to be aware of certain events and transactions that occur subsequent to the end of the fiscal year, but prior to the issuance of the financial statements. Generally, if a debt investment's credit rating is downgraded during this time period, it may constitute a "subsequent event" subject to disclosure. GAAP require disclosure of a subsequent event when the omission of the disclosure would cause the financial statements to be misleading.

According to *GASB's Statement 40 Implementation Guide*,³ governments should exercise professional judgment in determining whether or not a debt investment's credit rating downgrade is material to the government's financial statements and thus, subject to disclosure. Oftentimes, a government's investment policy or applicable statutory provisions may restrict a government from having a large credit risk exposure in a single entity's investment (concentration of credit risk). Generally, when a single entity's investment is downgraded, the government would not need to disclose the credit rating downgrade. However, if a government has a concentration of credit risk in a single investment, a credit rating downgrade may expose the government to a significantly higher level of credit risk; and therefore the government should disclose the credit rating downgrade as a subsequent event. For example, if the bankruptcy of a bond issuer causes a government's investment bond to be downgraded, it may indicate a large investment loss for the government. If the value of the investment is significant to the government's total investment portfolio, disclosure of such an event may be required.

³ Derived from NCGA Interpretation 6, *Notes to the Financial Statements Disclosure*.

If you have any questions regarding the information presented in this Bulletin, please contact the AOS Accounting & Auditing Support Group at (800) 282-0370.

A handwritten signature in black ink that reads "Betty Montgomery". The script is fluid and cursive, with the first letter of each word being capitalized and prominent.

Betty Montgomery
Ohio Auditor of State