



## ACCOUNTING

# Arrested Development

GASB defers a clarification but foreshadows future change

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**C**onsider, if you will, the variety of reasons governments own real estate (land and buildings). Real estate provides spaces for governments to administer their services, such as police stations, administrative office buildings, and recreation centers. Some governments may also hold real estate as a mechanism for generating income or in the expectation that the value of the holdings will increase over time, such as rental properties owned by pension funds for the purpose of diversifying their investment portfolios. Governments may also purchase real estate for economic and community development purposes in their jurisdictions, such as purchasing adjoining, run-down properties with the intent to sell them for redevelopment.

Governments have traditionally reported real estate three different ways: capital assets, investments, or assets acquired for resale.



## Capital asset

A tangible or intangible asset that is used in the government's operations and has a useful life of more than one year is reported as a capital asset. Capital assets are reported at historical cost, net of accumulated depreciation/amortization. Governmental funds do not report capital assets. Common examples include the city hall, fire station, and water utility plants.



## Investment

At the time of purchase, if the real estate property is primarily held for the purpose of income or profit and has a present service capacity based solely on its ability to generate cash or to be sold to generate cash, it meets the definition of an investment.<sup>1</sup> Such investments are measured and reported at fair value in the fund-level and entity-wide financial statements. Examples include commercial and residential rental properties.<sup>2</sup>

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### Asset acquired for resale

When real estate is purchased by a government with the intent to sell it to a third party, it is prevalent practice to report the real estate as a financial asset.<sup>3</sup> While this conclusion is not clearly supported in authoritative guidance,<sup>4</sup> governments have analogized inventory guidance to report these as assets on the fund-level [both governmental and proprietary] and entity-wide financial statements, at the lower of cost or net realizable value.<sup>5</sup> Common examples include redevelopment properties.

Governmental Accounting Standards Board (GASB) Statement No. 104, *Disclosure of Certain Capital Assets*, requires governments to identify and disclose the historical cost and accumulated depreciation of capital assets held for sale by major class of capital assets, while still including them within the “roll-forward” schedule within the appropriate major classes of capital assets. Capital assets held for sale are those that the government has made the decision to sell and for which the sale is likely to occur within one year of the financial statement date.<sup>6</sup> When GASB 104 was issued, the authors discussed whether the disclosure requirements for capital assets held for sale affected real estate assets acquired for resale. And, at the time, they believed them to be separate concepts. Then a new development altered the discussion and GASB Exposure Draft (ED) entitled *Implementation Guidance Update—2025* [IG Update].

On March 19, 2025, GASB re-deliberated the content of the anticipated IG Update based on comments staff

received on the ED, which had been issued for public comment in November 2024. The board tentatively<sup>7</sup> decided at that meeting not to object<sup>8</sup> to the issuance of several of the sets of questions and answers (Q&As) that had been proposed in the ED without changes, to accept staff-proposed changes to other Q&As, and to eliminate a few Q&As that the staff recommended dropping. Here we’ll look at one specific Q&A set that was left on the cutting room floor but is likely to reemerge in an already-planned sequel.

### What was proposed?

Paragraph 4.3 of the ED read as follows:<sup>9</sup>

Q—A government purchases a piece of real estate [land and a building] as part of an economic development activity. The government plans to sell the real estate and will not use it for any other purpose in the meantime. How should the real estate be reported?

A—Because the assets were purchased for economic development, they do not meet the definition of an investment. Economic development is a service provided by the government, and, therefore, purchasing and selling real estate for economic development is part of the government’s operations. Accordingly, the land and building should be reported as capital assets because they are assets used in operations and have useful lives greater than a single reporting period, which are the two characteristics of a capital asset described in paragraph 19 of Statement No. 34, *Basic Financial Statements—and Management’s Discussion and Analysis—for State and Local Governments*, as amended. The government also should

evaluate whether the land and building are capital assets held for sale as described in paragraph 5 of Statement No. 104, *Disclosure of Certain Capital Assets*.

The proposed answer had some wide-ranging implications and was a surprise to many. Specifically eyebrow raising were:

- The assertion that assets purchased with the intention of being sold as part of an economic development program are capital assets, and
- The implied assertion that the only two possible classifications of real estate assets owned by a government would be either investments or capital assets.

### What was the feedback?

The comments GASB received about this Q&A clearly reveal that there is diversity in how such assets are currently reported by governments.<sup>10</sup> Several of the comments received by GASB in response to the ED specifically addressed this Q&A. They pointed out that many governments treat capital-type assets that are acquired for resale, like inventory (as discussed above), by reporting them in both governmental funds and government-wide financial statements at either lower of their cost or estimated fair value (or estimated net realizable value).<sup>11</sup> Some even questioned whether this type of authoritative guidance should be made in a GASB Statement, which is Level A GAAP, instead of via an implementation guide, which is the lower Level B GAAP.<sup>12</sup>

GFOA’s comment letter on the ED expressed disagreement. Moreover, the proposed answer would partially contradict the nonauthoritative accounting guidance provided in GFOA’s publication, *Governmental Accounting, Auditing, and Financial Reporting* (a.k.a. the “GAAPFR” or the “Blue Book”) which states, in part:

Assets acquired for the purpose of sale (foreclosure properties, for example) or investments (real estate held by an endowment) do *not* qualify as capital assets, regardless of their form, because they are not *used in operations*....<sup>13</sup>

Many who provided comments on this Q&A in the ED, or who have discussed



it with the authors informally, also raised follow-up questions about topics including:

- How economic development is defined.
- How the estimated useful lives of acquired-for-resale capital assets would be determined for purposes of depreciation, or whether they should be depreciated at all.
- How governments would measure the value of such assets if they were donated or acquired as part of a foreclosure.
- Whether the capitalization of acquisition costs, or of the costs of any improvements made to these assets, should be limited by the assets' net realizable values.

## What did GASB decide?

As hinted earlier, during that March 19, 2025, board meeting, GASB tentatively endorsed removal of this Q&A; however, the board vote on the topic was not unanimous. More importantly, based on the discussion at that meeting, it seems we've not heard the last of this.<sup>14</sup>

GASB staff and virtually all the GASB board members expressed the beliefs that:

1. Real estate assets acquired for resale for economic development are capital assets, as the proposed answer had stated, and
2. That the *only* reason *not* to include the Q&A in the final IG Update was the expected benefit of answering the related questions and at the same time making this clarification.

## What should governments be thinking about now?

Governments that own capital-type assets that (1) were acquired for resale, (2) are not held as investments, and (3) are not reported as capital assets, should prepare for the likelihood that they will need to change their accounting going forward. Luckily, many such assets currently held may be sold before any forthcoming pronouncement on the topic would become effective.

Governments can take this opportunity to review their acquisitions of capital-type assets for resale, consider the impact of reporting these as capital assets, and ready themselves for potential ongoing discussions on this topic.

A change in reporting would cause fluctuations in the governmental funds flows statement. Capital assets are not reported in governmental funds. If the asset acquired for resale was purchased by a governmental fund, the acquisition would be reported as an expenditure in the year acquired. The subsequent sale proceeds would be reported as another financing source in the year of sale.

Using current accounting policies, governments should review the valuation of real estate purchased for resale and whether the result is a representationally-faithful measurement of these capital assets. For example, if a held-for-sale capital asset is expected to be held for only a short time, or its service capacity is not expected to diminish before resale, depreciation may be immaterial or simply not applicable.<sup>15</sup> In that scenario, a government would depreciate the difference between the asset's cost and that salvage value over the time the government the expected hold it. If improvements are made that are not expected to increase that "salvage" value, they too could be depreciated over the expected holding period.

## Conclusion

While there is no immediate action that governments must take, there is a pretty clear indication that the removal of this IG Update Q&A is not the last we will hear about the measurement and classification of assets acquired for resale. We know this would affect at least some governments, and GFOA will need to make some changes of our own. ■

<sup>1</sup> GASB Cod. Sec. 150, "Investments," paragraph 103.

<sup>2</sup> GASB Statement No. 87, *Leases*, includes a specific guidance for leases of assets held as investments by government lessors. If the asset meets the definition of an investment, government lessors should value and report the asset as an investment.

<sup>3</sup> *Governmental Accounting, Auditing, and Financial Reporting*, GFOA, 2024 Edition, Chapter 22, page 12-7.

<sup>4</sup> GASB Cod. Sec. 1800, paragraph .742-5 indicates that "properties held for resale" are reported on the governmental fund balance sheet and the resulting fund balance classification is restricted, committed, or assigned.

<sup>5</sup> This is likely based on analogy to guidance applicable to inventory assets held by proprietary funds and business-type activities found in GASB Codification of Governmental Accounting and Financial Reporting Standards, Section 140, originating from GASB Statement No. 62.

<sup>6</sup> GASB 104, paragraph 5.

<sup>7</sup> All GASB decisions are considered tentative until a final pronouncement is issued.

<sup>8</sup> GASB's implementation guidance is technically issued by GASB staff, after the board members vote not to object to its issuance. Implementation guidance is part of a classification of generally accepted accounting principles (GAAP) called "Level B" that is authoritative but subordinate to "Level A" GAAP, the latter of which includes GASB Statements and is formally promulgated when a majority of board members approve issuance.

<sup>9</sup> GASB 2025 IG Update ED, paragraph 4.3.

<sup>10</sup> CliftonLarsonAllen LLP, AICPA SLGEP, Baker Tilly US LLP, GFOA.

<sup>11</sup> Alternatively, the lower of cost or net realizable value.

<sup>12</sup> See footnote 2.

<sup>13</sup> *Governmental Accounting, Auditing, and Financial Reporting*, Chapter 22, page 22-1.

<sup>14</sup> At the time of this writing, GASB's website ([gasb.org/news-and-meetings/past-meetings](https://gasb.org/news-and-meetings/past-meetings)) contains a link to a video recording of the March 19, 2025, meeting. The redeliberation of this proposed Q&A begins at approximately 1:14:30 and lasts approximately 24 minutes.

<sup>15</sup> A reasonable question would be why the expected holding period, rather than the much longer period during which a capital asset will have utility (for example, the building may be serviceable for 30 years from the date of acquisition and the land likely will be serviceable forever), and should be considered its useful life.



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