3.2 **Assets**

3.2.8 **Joint Ventures**

3.2.8.10 Local governments may cooperate under certain conditions with other local governments. The basis is for mutual advantage to provide services and facilities. This is accomplished in a manner and pursuant to forms of governmental organization that will accord best with geographic, economic, population, and other factors influencing the needs and development of local communities.

3.2.8.20 All cooperative efforts created by State law can be joint ventures. All joint ventures are either joint operating agencies or contracted interlocal agreements. Specific laws dictate other limitations or requirements, depending on the purpose and entity. Descriptions of some cooperative efforts are as follows.

Joint Operating Agencies (Chapter 43.52 RCW and Chapter 54.44 RCW)

3.2.8.30 A joint operating agency (JOA) is a legal entity created between any two or more cities or public utility districts. This agency is a municipal corporation of the state of Washington. A JOA has authority to enter into contracts involving electric energy, fisheries, flood control, and natural resources.

3.2.8.40 Management and control of a JOA vests with the board of directors. The directors are appointed by the legislative body of each member of the JOA.

3.2.8.50 For guidelines and requirements, see Chapter 43.52 RCW for operating agencies and Chapter 54.44 RCW for nuclear power plants.

3.2.8.60 For accounting treatment, joint operating agencies should be treated as a public utility district (RCW 43.52.391).

Interlocal Agreements (Chapter 39.34 RCW)

3.2.8.70 An interlocal agreement is a contract entered into between two or more public agencies for joint or cooperative action. This action must be a power, privilege, or authority already capable of being exercised by the public agencies involved, and the manner of financing should be as provided by law. The agreement could establish a separate entity as described below.

3.2.8.80 If the interlocal agreement does establish a separate legal or administrative entity, this entity must be legally created (Insurance Boards RCW 48.62.041, RCW 48.62.101, Irrigation Districts RCW 87.03.018, Hydroelectric Resources RCW 87.03.828). The agreement must specify duration, organization, purpose, manner of financing and methods of termination. Funds of this separate entity would be subject to audit in the manner provided by law for the auditing of public funds.

3.2.8.90 If the interlocal agreement does not establish a separate legal entity by law, the agreement must specify the criteria listed above and must also provide for an administrator or a joint board responsible for administering the cooperative undertaking. Provisions are also required to detail the manner of the joint board in acquiring, holding, and disposing of real and personal property used in the joint undertaking. The joint board is also authorized to establish an operating fund with a county, city, or district treasurer of one of the involved public agencies.

3.2.8.100 The interlocal agreement is filed with the county auditor, and if applicable, a state officer or agency with statutory powers of control.

Chapter 39.34 RCW issues various guidelines and requirements applicable to interlocal agreements.

3.2.8.110 For accounting treatment, an interlocal agreement must be evaluated for each member agency to determine whether joint venture treatment is applicable. If joint venture treatment is applicable, see the accounting treatment below. If joint venture treatment is not applicable, interlocal agreement should be footnoted and accounted for in an appropriate fund. Contractual requirements take precedence over accounting requirements (i.e., a contract may require one member to be reporting entity when it does not exercise "oversight responsibility").

Accounting Procedures for the Joint Ventures

3.2.8.120 GASB Statement 14, *The Financial Reporting Entity* defines the joint venture as a legal entity or other organization that results from a contractual agreement and is owned, operated, or governed by two or more participants as a separate and specific activity subject to joint control, in which the participants retain an ongoing financial interest or an ongoing financial responsibility.

3.2.8.130 Joint control means that no single participant has the ability to unilaterally control the financial or operating policies of the joint venture.

3.2.8.140 Ongoing financial interest means an equity interest or any other arrangement that allows a participating government to have access (directly or indirectly) to joint venture's resources.

3.2.8.150 Ongoing financial responsibility means that the participating government is obligated in some manner for the debts or the funding of the joint venture.

3.2.8.160 Lack of the ongoing financial interest or the ongoing financial responsibility designates the entity as a jointly governed organization, subject to different disclosure requirements.

3.2.8.170 When the number of participants in a joint venture increases their financial responsibility may decrease. Statement 14 does not establish any break point for the determination if the participant is financially responsible or not. A decision, in the marginal cases, is left to the professional judgment of the government.

3.2.8.180 For financial reporting purposes there are two types of joint ventures:

1. Joint ventures whose participants have equity interest.
2. Joint ventures whose participants do not have equity interest.

3.2.8.190 The indication of an equity interest is an ownership of shares of the joint venture's stock or other explicit and measurable rights to net resources (usually based on investment of financial or capital resources in the joint venture). To be considered explicit and measurable the rights to the present or future claims to the joint venture's resources and the methods to determine the amounts have to be clearly defined in the joint venture agreement. If equity interest in the joint venture is implied rather than explicitly stated the joint venture participants should consider modifying the agreement to clarify its intent.

Reporting Equity Interest in Joint Venture:

3.2.8.200 The proper accounting and financial reporting for joint ventures depends on whether the underlying contract creates an explicit, measurable equity interest in some or all of the joint venture's resources. If there is an explicit, measurable equity interest in the joint venture, the government's investment in the joint venture should be reported as a single line item in the government-wide statement of activities. The same treatment applies to the proprietary fund financial statements.

3.2.8.210 In the case of governmental funds, however, an investment in the joint venture should be reported in a governmental fund only to the extent that it represents a financial asset rather than an interest in the underlying capital assets of the joint venture. Joint ventures not involving an explicit, measurable equity interest are reported simply as note disclosures.

3.2.8.220 The following examples illustrate how the provisions of the GASB Statement 14 would be applied to a particular set of hypothetical circumstances.

Example 1: Twin City Airport Authority

Facts: The Twin City Airport Authority was created jointly as a separate legal entity by two cities. At inception, City A contributed 60 percent and City B contributed 40 percent of the initial capital (to purchase land). The cities jointly issued construction revenue bonds and facility revenue bonds to finance construction of the airport. The construction bonds are payable solely from and secured by airport revenues, and the facility bonds are payable solely from and secured by net rent revenues payable from various leases. The cities are not obligated in any manner for the authority debt. The initial capital investments of the two cities are to be returned to the cities by the authority over a period of time not to exceed fifteen years.

The authority is governed by a ten-member board composed of the mayor of each city and three members of City B's city council and five members of City A's city council. Despite the numerical imbalance of the board, the joint venture agreement provides for joint control; that is, both cities must approve the budget, the issuance of debt, and other significant activities.

The cities individually have executed covenants, by ordinance, to levy a maintenance tax (subject to rate limitations) if necessary to insure that the airport will be operated and maintained efficiently. The authority board has entered into agreements with each airline that uses the airport, providing for adjustments to rentals, fees, and other charges that management believes would preclude losses from being incurred. To date, no maintenance tax has been levied by either city, and the airport has generated sufficient revenues to make annual payments to the cities in accordance with the repayment agreement for their initial capital contributions.

Conclusions: The airport authority is a joint venture because it was created as a separate legal entity and both cities have on ongoing financial responsibility for the entity. The fact that City A appoints a numerical majority of the authority's board is negated by the two cities' agreement for joint control of the authority. The initial capital contributed by the cities has the characteristics of an equity interest, but the agreement with the airport authority, in effects, converts the equity interest to a long-term receivable. Therefore, rather than reporting an equity interest in the joint venture in the general capital assets, the cities would report a receivable in the fund that receives the annual payments from the authority. The cities do, however, have ongoing financial responsibilities for the authority because they have obligated themselves to fund the deficits of the airport by agreeing to levy maintenance tax if needed. The cities would make the required joint venture disclosure.

Example 2: Bi-State Port Authority

Facts: Two state governments create a port authority as a separate legal entity. Each state appoints six governing board members for the authority; the chairperson is elected by the twelve members from within the board. the authority is autonomous from a day-to-day operations perspective. Neither state provides start-up funds; the authority's facilities were financed with its own revenue bonds.

Neither state is obligated for the authority's debt and neither state is obligated for its deficits or entitled to its operating surpluses, either directly or indirectly. The authority is financially self-sufficient. It is perpetual and no provisions are made in its charter or by-laws for the distribution of assets at termination.

Conclusions: The authority is a jointly governed organization. It is not a component unit because neither state appoints a voting majority of the authority's governing board. It is not a joint venture because the states do not have an ongoing financial interest or responsibility for the authority. If, however, the states could influence the management of the authority (through veto power over the authority's decisions regarding major projects, for example) to undertake projects that would benefit the states, an ongoing financial interest would exist and them authority would be considered a joint venture. In either case, the states should make the appropriate disclosures about their relationship to the authority.

Example 3: Municipal Electric Authority

Facts: Forty-eight cities have formed a municipal electric authority as a public corporation according to state law. The purpose of the authority is to enable small municipal electric systems to efficiently finance, construct, and operate electric power generation and transmission facilities. Each participating city appoints one member to the authority's governing board. Construction of the authority's facilities was financed by revenue debt of the authority. None of the participants is in any way liable for the authority's debt. The authority bills each participant for usage at rates that are calculated to cover the authority's *cost* as defined in the bond indenture. The rates are structured to systematically provide cash for debt requirements, operating expenses (excluding depreciation and amortization), and reserves as specified by the bond indentures. Each city is bound by contract with the authority to annually purchase a minimum number of kilowatt-hours. The contracts are renewable at the cities' option every three years. Except for the minimum purchase contracts, no participant has any other obligation, entitlement, or residual interest. The authority is financially self-sufficient.

Conclusion: The authority should be reported by participants as a jointly governed organization. None of the participating municipalities has an ongoing financial interest, and because of the large number of participants the cities' purchase contracts with the authority do not represent ongoing financial responsibilities.