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November 22, 2011

David R. Bean, CPA
Director of Research and Technical Activities
GASB
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

Re: August 17, 2011 Exposure Draft (ED) of a Proposed Statement of the Governmental Accounting Standards Board, Reporting Items Previously Recognized as Assets and Liabilities [Project No. 3-23]

Dear Mr. Bean:

One of the objectives that the Council of the American Institute of Certified Public Accountants (AICPA) established for the PCPS Executive Committee is to act as an advocate for all local and regional firms and represent those firms' interests on professional issues, primarily through the Technical Issues Committee (TIC). This communication is in accordance with that objective. These comments, however, do not necessarily reflect the positions of the AICPA.

TIC appreciated the opportunity to discuss its preliminary views on the ED with the GASB Chair and staff at the September 26, 2011 GASB/TIC Liaison Meeting and is now providing the following written comments for your consideration.

### **GENERAL COMMENTS**

Although TIC agrees with many of the classification decisions presented in the ED, TIC has concerns about certain proposed changes that seem inconsistent in relation to current established practices, may be cost prohibitive for preparers or may be confusing to financial statement users. These concerns are discussed in detail below.

Appendix C is a very useful feature and should be retained and added to the GASB Comprehensive Implementation Guide.

Selected TIC members discussed this proposal with some of their clients and found that most either do not understand or question the usefulness of many of the classification changes. During the transition phase for the final standard, TIC encourages the Board to prepare extensive educational materials, particularly for governments and financial statement users, to explain the captions and to ensure all constituents understand why

these changes are necessary, how the changes are expected to change practice, and what users need to consider as they review governmental financial statements.

### **SPECIFIC COMMENTS**

## **Imposed Nonexchange Revenue Transactions**

Paragraph 9 states in part, "Deferred inflows of resources should be recognized when resources are received or recognized as a receivable before (a) the period for which property taxes are levied...." TIC believes this paragraph is overly complex and could be misinterpreted. TIC recommends the paragraph be revised to more clearly articulate the Board's intent and suggests the following:

Deferred inflows of resources should be recognized when **cash** is received or receivables are recognized before (a) the **applicable property tax** period, or (b) the period when resources are required to be used or when use is first permitted for all other imposed nonexchange revenues in which the enabling legislation includes time requirements. (Suggested changes are in boldface type.)

# Government-Mandated Nonexchange Transactions and Voluntary Nonexchange Transactions

Under GASB Statement (GASBS) No. 33, Accounting and Financial Reporting for Nonexchange Transactions, funds provided in advance are generally classified by the recipient as a liability (deferred revenue) whenever any of the eligibility requirements has not been met. (An exception to this rule exists if the time requirement meets the criteria in paragraph 22 of GASBS No. 33.) The proposal would amend GASBS No. 33 to require a recipient to report a deferred inflow of resources whenever resources are received or recognized as receivable and the time requirements are the only eligibility requirements that have not been met. The effect of the proposed amendment would force provider and recipient governments to track all time requirements separately from other eligibility requirements. Under current standards, only the special time requirements discussed in paragraph 22 of GASBS No. 33 are accounted for differently from other eligibility requirements.

TIC believes the excess cost and time commitment necessary to recognize an asset or liability for one and a deferred outflow/inflow for the other would far exceed any perceived benefits for financial statement users. One TIC member discussed this proposed requirement with one of her university clients. The additional requirements to track and record the deferral of grant revenue depending on eligibility and timing would be of no value to the reader. The client expressed concern that such deferrals will be very confusing to financial statement users. In addition, with budget cuts and little staff, any additional requirements to differentiate between two different financial statement elements (e.g., liabilities v. deferred inflows of resources) add no value, but would add time commitments that preparers don't have. The greatest burden would fall on the

finance department, since grants come from many different departments within the university.

TIC recommends that the Board establish deferred inflows and outflows only where they are truly needed. Otherwise, the financial statements may become less transparent from the user's perspective. Given the limited usefulness of this information and the cost issues associated with this proposed requirement for universities that receive state grants or a county government that is getting state funds, etc., TIC believes this aspect of the ED is without merit. TIC recommends that any resources provided/received before all eligibility requirements are met should be classified as deferred outflows/deferred inflows.

### **Debt Issuance Costs / Debt Refunding**

TIC believes the Board's position on accounting for debt issuance costs is inconsistent with its position on accounting for the gain/loss in a refunding of debt. Paragraph 15 states that all debt issuance costs (except for prepaid insurance) should be recognized as an outflow in the period incurred. However, paragraph 6 would effectively require that the gain or loss in a debt refunding transaction be reported initially as a deferred inflow or deferred outflow of resources.

TIC believes there is no identifiable difference between these two types of items and therefore disagrees with the Board's proposal to require recognition of an outflow in the period debt issuance costs are incurred. TIC believes that the issuance costs incurred and gain/loss recognized cannot be separated from the underlying debt instrument. To separate them and account for them differently would be very confusing to users and preparers of financial statements and not provide an accurate representation of the actual cost of the debt instrument.

Many governmental entities operate under a business reporting model, rather than a governmental model. One TIC member's client, upon learning of this ED, expressed concerns about the many changes proposed in the ED and the resulting lack of comparability with its private sector counterparts.

Therefore, TIC cannot support two different classifications for transactions that are essentially very similar. TIC recommends that these items continue to be capitalized, and that debt issuance costs not be expensed as incurred. TIC believes all debt issuance costs should be classified as deferred outflows, and gains/losses on refundings of debt should be classified as deferred inflows/deferred outflows, as appropriate.

### **Loan Origination Fees/Costs**

TIC does not support the proposed change in classification for loan origination fees received and loan origination costs paid in connection with lending activities or a mortgage loan held for investment. Under the proposal, such loan origination fees (except for any portion relating to points, which would be classified initially as a deferred inflow

of resources) would be recognized in revenue as an inflow of resources in the period received. Similarly, loan origination costs relating to lending activities or mortgage loans held for investment would be recognized as an expense (outflow) when incurred.

TIC believes loan origination fees/costs represent adjustments to yield for loans held for investment. For this reason, they are applicable to future periods and should be capitalized and amortized over the life of the loan. Loan origination fees are defined in GASBS No. 62, paragraph 451, as "fees charged to the borrower in connection with the process of originating, refinancing, or restructuring a loan." Such fees have always included points, as well as a number of other specific costs. TIC believes the classification of all cost elements should be the same. Points should not be the only element that is eligible for deferral over the life of the loan.

TIC therefore believes all loan origination fees received should be classified as deferred inflows of resources, and all loan origination costs should be classified as deferred outflows of resources.

TIC members do not have direct experience with clients that hold mortgage loans for sale. Therefore, no comments are provided on this aspect of the proposal.

# Circumstances in Which a Pension Plan's Net Position Exceeds the Total Pension Liability

TIC also disagrees with the Board's conclusion that excess plan net position should be classified as a prepaid expense (paragraph 49 of the ED). TIC believes the relationship between the plan net position and the total pension liability is not analogous to a prepayment since the excess will be paid to current retirees and cannot be taken back by the government. The plan does not have true "excess cash" because the excess occurred due to the long amortization period that is applied to the total pension liability. Considering the excess an asset would not, in TIC's view, represent an appropriate interpretation of the definition of an asset per GASB Concepts Statement No. 4, *Elements of Financial Statements*. TIC therefore recommends that the excess be classified as a deferred outflow of resources.

# Appendix C—Listing of Classification of Items and Markup of Paragraphs That Are Significantly Modified

TIC appreciated the inclusion of this appendix in the ED. A detailed synopsis of the particulars of a standard is always very helpful. The list of classifications is a very important addition since it is the only place in the ED that includes a concise summary of the Board's decisions on reporting items previously recognized as assets and liabilities.

The markup of extant standards that will be significantly modified by this proposal is also very helpful in understanding the nature of the many proposed changes.

TIC recommends both items be carried forward to the GASB Comprehensive Implementation Guide once the standard is finalized. TIC believes this is valuable reference material that will be consulted frequently—even after the standard becomes effective.

TIC appreciates the opportunity to present these comments on behalf of PCPS member firms. We would be pleased to discuss our comments with you at your convenience.

Sincerely,

Karen Kerber, Chair

Karen Kerber

**PCPS Technical Issues Committee** 

cc: PCPS Executive and Technical Issues Committees