

To: Director - GASB

Subject: Pennsylvania's comments on GASB Preliminary Views Document "Fair Value Measurement and Application"

Good afternoon Dave,

We are pleased to provide comments on the Governmental Accounting Standards Board's (GASB's) Preliminary Views (PV) of the major issues related to Fair Value Measurement and Application which was issued June 3, 2013.

We believe a single definition of fair value, together with a framework for measuring fair value, should result in increased consistency and comparability in fair value measurements. Also, the expanded disclosures of fair value measurement should provide users of financial statements with better information about the extent to which fair value is used to measure recognized assets and liabilities and the inputs used to develop the measurements. Conceptually, financial reporting should evolve towards reporting more current values—that is, values that are relevant to the entity and reflect economic circumstances at the balance sheet date. However, in many cases, for practical considerations, historical cost should continue to be used. Compliance with the proposed changes has the potential to add significant internal personnel costs as well as external costs for auditors and outside valuation experts, placing an unnecessary burden on governments already over committed staff.

Issue 1—Definition of Fair Value

It is the Board's preliminary view that the definition of fair value should be the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. (See Chapter 2, paragraphs 3–6.) Do you agree with this view? Why or why not?

We agree in part with the board's preliminary view. The definition of fair value should be consistent with other standards setters. However, we believe that historical cost should continue to have pre-eminence in the valuation process. We have three concerns as follows: 1) to ascertain the fair value of various assets periodically will be very burdensome on the government sector in view of the current reductions in budgets and staffing; 2) ascertaining fair value can be a lengthy endeavor which contradicts efforts to achieve quicker issuance of financial statements and; 3) chapter 2, ¶24 gives the reporting entity the ability to disregard a transaction or quoted price and use unobservable inputs, if the entity deems the market value "does not represent fair value", (level 3 input).

To analyze fair value annually is cost prohibitive and time inefficient. Staff requirements and possibly the cost of an outside vendor, to evaluate assets annually would put a burden on government resources that are already taxed to their limits. Paragraph 11 states, "The Board recognizes that obtaining fair value information for use in preparation of the financial statements (including disclosures) may take more time than other measurements (such as historical cost). However, the Board believes that delays in financial reports generally should not be significant enough to outweigh the usefulness of fair value information." The board concurs it will take more time and take longer. Historically the board has underestimated the amount of time it requires to implement new standards and this standard in particular will require significant amounts of time and effort.

The standard promotes the subjective defining of what is not an orderly transaction. Per ¶24 a reporting entity may choose to disregard the value if it deems the "transaction or quoted price does not represent

fair value”, namely because the market was “not orderly”. The following paragraph gives examples of what transactions are not orderly. The first two examples, ¶25a and b, both are dependent on the reporting entities discretion. The reporting entity can manipulate the situation by marketing to a single market participant or limiting market exposure and then declare, “the transaction is not orderly” to justify using subjective fair values, level 3 inputs. Paragraph 25a and b should be eliminated or redefined.

Issue 2—Transaction Costs

It is the Board’s preliminary view that transaction costs to sell an investment should be treated as period costs. That is, transaction costs would not be a reduction of an investment’s fair value in the statement of financial position. Transaction costs would be reported as expenses or expenditures in the period an investment is sold. (See Chapter 2, paragraphs 21 and 22.) Do you agree with this view? Why or why not?

Agree. Transaction costs do not meet the definition of assets or deferred outflow of resources.

Issue 3—Definition of an Investment

It is the Board’s preliminary view that the definition of an investment should be a security or other asset that a government holds primarily for the purpose of income or profit, and its present service capacity is based solely on its ability to generate cash, to be sold to generate cash, or to procure services for the citizenry. (See Chapter 3, paragraphs 2–4.) Do you agree with this view? Why or why not?

We agree with the boards proposed definition of investments.

Issue 4—Measurement of Investments

It is the Board’s preliminary view that investments generally should be measured at fair value on a recurring basis. (See Chapter 3, paragraphs 14–16.) Unless specifically excluded from a fair value measurement, investments would no longer be valued using amortized cost or other measures. (See Chapter 3, paragraph 19.) Do you agree with this view? Why or why not?

We agree with the board, that investments should be measured at fair value as a general rule because amortized cost measurements have the potential to mislead financial statement users. Also, we agree that only specific assets addressed in chapter 3 ¶16 of this PV should continue using the amortized cost measurement.

Issue 5—Disclosures

5a. It is the Board’s preliminary view that the disclosures discussed in Chapter 4 should be required. Are any of the proposed disclosures not essential to a financial statement user’s understanding of financial position or inflows and outflows of resources? Why or why not?

We generally agree with the disclosures addressed herein by the board with a few notable exceptions.

Chapter 4¶10 states, “If a fair value is developed by a pricing service, there would be no requirement to disclose significant assumptions if the pricing service considers those assumptions to be proprietary and, after a government makes a reasonable effort, the pricing service declines to make that information available. This fact, however, would be disclosed.”

This exception goes in opposition to the concept of transparency in disclosure. One cannot evaluate whether a method is fair value if the pricing service will not disclose the detail. We believe there should be a certain amount of detail that is required to be disclosed by the pricing service in order for the financial statement users to evaluate if in fact, the method is reasonable.

Lastly, chapter 4¶11 states, "To comply with the above disclosure requirement, the narrative description of the sensitivity to changes in unobservable inputs would include, at a minimum, the unobservable inputs disclosed when complying with paragraph 9a(2) of this chapter." We agree a certain level of narrative be required to disclose the unobservable inputs that materially/significantly affect the fair value.

5b. What other disclosures related to fair value should the Board consider? Why?
No other disclosures are noted.

The proposed changes in this PV will increase consistency and comparability in government's fair value measurement and related disclosures. We appreciate the opportunity to comment on this Preliminary Views document and hope you find our comments helpful. Please contact me with any questions at mburns@pa.gov or Anna Maria Kiehl at akiehl@pa.gov or (717) 787-6496.

Have a great afternoon!
Mike

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