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November 14, 2011

Mr. David Bean
Director of Research
Governmental Accounting Standards Board
401 Merritt 7
Norwalk, CT 06856-5116

Dear Mr. Bean:

On behalf of the National Association of State Auditors, Comptrollers and Treasurers, we appreciate the opportunity to respond to the Governmental Accounting Standards Board's Exposure Draft (ED), *Reporting Items Previously Recognized as Assets and Liabilities*.

We believe this ED satisfactorily addresses the need to classify certain assets and liabilities under the Concept Statement No. 4 categories of deferred inflows of resources and deferred outflows of resources. While we generally agree with the provisions included in the ED, we have the following specific comments that we believe the board should consider as it finalizes this statement.

Paragraph 3

Several of the paragraphs not identified as applicable to governmental funds address transactions that we believe would produce reportable activity for governmental funds (whether assets/liabilities, deferred, or currently recognized). Examples include debt issuance costs (paragraphs 14 and 15), acquisition costs for insurance activities (paragraphs 19 and 20), lending and mortgage activities (paragraphs 22-27). Only paragraphs 28 and 29 on regulated operations specifically limit their applicability to business-type activities. If the Board has concluded that paragraphs 14-15 and 19-27 represent activity that can only occur in nongovernmental funds then that should be stated; otherwise, we believe those paragraphs should also be identified as applicable to governmental funds.

Paragraph 33

We agree with the guidance that requires combining deferred outflows of resources with assets and combining deferred inflows of resources with liabilities when determining whether those elements (assets or liabilities) meet the criteria for major fund determination. We believe this approach is appropriate since the combined amounts represent the fund's total resources available to provide service or the fund's total resources that are obligated.

Paragraphs 46-48 and 50-52

Items are identified that retain the classification as assets and liabilities respectively. Except for the attributes of refundability addressed in paragraphs 48 and 52, the document does not provide explanation or justification for the classification of these items as assets and liabilities. The text restates the Concept Statement No. 4 definition of elements rather than explaining how each of the identified transactions meets that definition. Given the hierarchy of classification established in paragraph 44, these items warrant explanation of how they meet the definition of assets and liabilities because that determination precludes them being considered for deferral or current recognition. For example, we do not believe prepaid items meet any of the three control criteria applicable to assets. Prepaid subscriptions, insurance and rent all are intrinsically related to future periods that would preclude present capacity to provide services to citizens, in most instances they cannot be exchanged for another asset, and there is no alternative way to use the prepaid item to provide service benefit.

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Paragraph 47

The intent of the cross reference to paragraph 73 of NCGA Statement No. 1 is unclear. The text of paragraph 73 addresses prepaid items as an alternative recognition method that is “usually of a relatively minor nature” in allowing the item to be expensed rather than capitalized as an asset. If this reference is solely to provide a standards-based recognition of the prepayment concept that should be made clear because the treatment discussed in NCGA Statement 73 does not appear to support the treatment required by paragraph 47.

Paragraph 62

The cases presented appear to be backward. When the value of resources required to refund old bonds is less than the carrying value, the result is a credit not a debit. The discussion in this instance should be about whether the credit represents a liability, a deferred inflow, or gain, not whether it represents an asset, deferred outflow, or loss. When the value of resources required to refund old bonds is more than the carrying value, the result is a debit not a credit. The discussion in this instance should be about whether the resulting debit represents an asset, a deferred outflow, or a loss, not whether it represents a liability, deferred inflow, or a gain. Except for this technical issue we agree with the deferral of gain/loss on refunding.

Paragraphs 73 and 74

We do not agree with the conclusion about debt issuance costs. The lack of additional costs as an argument runs contrary to long established universal accounting principles. The reason for amortization (or possible deferred items) is because the costs are front loaded. Debt issuance costs were essential to either lowering future interest outflows or extending/shortening the debt service schedule; therefore, we believe these costs are applicable to future periods. Using the logic supplied, installation costs of a capital asset should be expensed in the period incurred rather than capitalized and depreciated over the life of the asset. In each of the instances where the Board has chosen current recognition of initial costs, it has cited a) the temporal nature of the transaction, b) the lack of subsequent similar costs, and c) completion of the transaction as the basis for reaching the conclusion to currently expense the transaction. We find these attributes to be of significantly less relevance than the accurate presentation of future gain/loss recognition in interest expense to be achieved through deferral and amortization.

Paragraph 74

By using the term “directly relate to future periods” we believe the Board has gone beyond the Concepts Statement No. 4 criterion that deferred items be applicable to future periods. The ED applies the “directly relate to future periods” criterion throughout.

Paragraph 78

The ED requires current recognition of loan origination fees. We disagree with this conclusion because we believe those fees are indistinguishable from compensation for surrendering the opportunity to use the funds for other investments in the future. In addition, a lending activity inherently is related to future periods, and we believe it is incorrect to consider administrative costs of loan issuance to be related to only one of those periods. Although it may not be practical or cost beneficial to defer and recognize these fees over time, avoiding deferral on a theoretical basis in interperiod equity will further degrade understanding of that concept. We believe the Board will achieve more consistent understanding and application of this proposed standard if it allows current recognition of loan origination fees (and other initial costs and fees) based on cost benefit and lack of materiality rather than arguments around applicability to a single period.

Paragraph 81

The reference in this paragraph to paragraph 56 is confusing. Paragraph 56 does not specifically address commitment fees, but rather, it generically addresses the impracticality of segregating a large number of transactions between the transaction price and performance obligation cost (for the purpose of potentially deferring the difference to be earned in future periods). Perhaps the reference should be to another paragraph. Or perhaps paragraph 27 should be rewritten to state that the generic discussion of

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performance obligations (that is, being treated solely as liabilities rather than partially deferred) applies to commitment fees.

Paragraph 82

We agree that commitment fees should be recognized as revenue when the commitment expires unexercised and when the probability of exercise is remote. However, we do not agree that there is a theoretical basis in interperiod equity for recognizing commitment fees in the initial period rather than deferring them. We believe the commitment fees constitute compensation for foregoing the future opportunity to invest in other activities. For similar reasons we disagree with current recognition of fees and costs related to purchases of loans (paragraphs 84 and 85) and mortgage loan origination fees (paragraphs 87 and 90).

Paragraph 98

We agree with the deferral of gains that reduce net allowable costs. However, we believe the Board should specify whether that recognition occurs over the remaining life of the early extinguished debt or over some other period.

Paragraph 104

We are unclear of the meaning of the third sentence in the paragraph. We recommend stating that not including deferred items could cause funds with large deferrals to no longer be considered major funds, leaving smaller funds as major. Similar confusion also arises in the last sentence of paragraph 105.

Appendix C, Paragraph 113

We were unable to determine whether the items listed as continuing to be reported as assets and liabilities should be reported on both the economic resource measurement focus based statements and the current financial resources measurement focus based statements. For the third and fourth to last bullets of the liabilities section, loan commitment fees (related to paragraph 23) and fees received for mortgage loan guarantees (related to paragraph 27) it is implied that these fees would not be reported on the governmental fund statements because paragraphs 23 and 27 are not marked as applicable to governmental funds. If the Board believes these two items, or any of the other items in the asset or liability sections, would only occur in proprietary funds or the government-wide statements, that should be stated. However, we do not believe that conclusion is correct, and as a result, additional paragraphs in the body of the ED should be identified as applicable to governmental funds. It seems inconsistent that many of the items listed in the asset and liability sections of Appendix C are only mentioned in the Basis for Conclusions and not in the body of the ED. Since this proposed standard is intended to designate transactions for specific treatment, we believe those transactions retaining their historical treatment should be addressed in the body not just the Basis for Conclusions and Appendix C.

We believe the Board should consider adding indicators to the classification of items in Appendix C to show whether each item is applicable at the government-wide, proprietary and fiduciary level only (economic resources focus) or if the item also is applicable at the governmental fund level (current financial resources focus).

We believe the following additions are needed to the Listing of Classification of Items:

- The reduction of revenue or the expense identified in paragraph 29a should be reflected as "Refunds imposed by a regulator" (paragraph 482 of Statement No. 62) in the section related to items that "should be reported as an outflow of resources" (page 32 of the ED) and/or the section related to items that "should be reported as an inflow of resources" (page 34 of the ED).
- Recognition by a regulated business-type activity of rates previously collected (and deferred) at the point in time that related costs have been incurred (paragraph 29b) should be included in the section related to items that "should be reported as an inflow of resources" (page 34 of the ED).

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General Comments

Although the nature and complexity of this proposed statement is more technical than theoretical, and less voluminous than others, the comment deadline still presented a challenge to financial statement preparers during a busy and critical time of the year.

The proposed effective date for the implementation of the statement seems ambitious. The implementation of other GASB statements, along with the fact that this statement is not finalized, leaves too little time to successfully implement such a complicated restructure.

We appreciate the opportunity to provide our comments. Should you have any questions or need additional information regarding our response, please contact Kim O’Ryan of NASACT at (859) 276-1147 or me at (334) 242-9200.

Sincerely,

A handwritten signature in black ink that reads "Ronald L. Jones". The signature is written in a cursive style with a large, stylized initial "R".

Ronald L. Jones
NASACT President