September 25, 2012

Director of Research and Technical Activities
Project No. 19-18
Government Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

Dear Director,

Please accept the following response from our appointed Accounting Standards Review Committee as official comment from the Oregon Municipal Finance Officers Association (OMFOA). We are responding to Governmental Accounting Standards Board’s (GASB) request for written comments to Exposure Draft Project No. 19-18: Accounting and Financial Reporting for Nonexchange Financial Guarantee Transactions.

The consensus of the committee is that the exposure draft provides needed guidance for accounting and financial reporting for nonexchange financial guarantees. The committee has some comments and recommendations that we believe should be considered before finalizing the statement.

**Component Unit Reporting.** Paragraph 4 notes that the scope and applicability should be applied to a “legally separate entity”. Until reading paragraph 25, committee members were unsure if the proposed statement would be applied to component units. Committee members would like the Board to reconsider applying the proposed statement to blended and discretely presented component units. Applying the proposed statement to component units could result in a doubling up of the liability. For example, a primary government extended a financial guarantee for a component unit’s debt and the component unit could not make the required debt payment. The primary government would be required to report the liability that is already reported in the component unit as debt, therefore doubling up this obligation. Please reconsider applying the proposed statement to component units.

The committee disagrees with the practice of “doubling up liabilities” within a financial reporting entity. The proposed standard should be changes so it requires a given financial reporting entity with intra-entity non-exchange financial guarantees to report and disclose only what is actually owed so there is no “doubling up” and no overstatement of liabilities. Overstating liabilities diminishes the comparability between financial statements and provides misleading financial information to users of financial statements which could very well likely have a material affect on the usefulness of financial information to users and decision makers. The financial reporting entity itself should report the liability at the amount that is actually owed; whereas, internally or in its notes it should disclose the debts between entities and the shared responsibility required to satisfy the one liability again for the actual amount owed. It is not appropriate and it is not reasonable to count a significant liability twice when two entities combine their financial statements into one report. If the rules of a financial reporting entity require overstating liabilities then they too will need to be questioned and/or redefined.

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Recognizing the Liability. Committee members are concerned that the government should recognize a liability and an expense in the financial statements when it is more than 50 percent likely that a government will make a payment on nonexchange financial guarantees it extended. The reliance on professional judgment in assessing probability will increase the burden of the government. Most small governmental entities do not have the time and resources to devote to reevaluating their nonexchange financial guarantees on an annual basis. In addition, the governmental entities auditors will have to attest to the probability to ensure that the potential liability is properly included or excluded from the financial statements. The consensus of the committee is that the liability and expense should not be included in financial statements until default occurred.

Committee members understand the need for transparency and recognition of the nonexchange financial guarantees in the financial statements. By disclosing the information listed in paragraphs 13(a), 14(a), 14(b), 14(c), 14(f), and 14(g) in the notes to the financial statements until default occurs, it will improve the recognition and disclosure for nonexchange financial guarantees.

Type of Guarantee. Committee members are unsure what “type of guarantee” is referring to in paragraph 13 and 14. Please include an example disclosure illustrating guarantees by type of guarantee.

Alternative View. Committee members believe that the information contained in this proposed statement is necessary since nonexchange financial guarantees are unique contingent liabilities. Committee members agree with the Board member who believes the Board should establish a separate project to readdress all aspects of governments contingent liability reporting.

Example. Committee members noted that an example of the disclosure required for the first year of a nonexchange financial guarantee prior to default should be included to ensure standardized/consistent reporting among governmental entities.

Committee members believe the guidance will improve the recognition and disclosures that governments have extended or received nonexchange financial guarantees. In addition, the proposed statement will enhance a users’ ability to assess the probability that governments will repay obligation relating to nonexchange financial guarantees.

We appreciate the opportunity to provide input on this exposure draft.

Sincerely,

Jeff White
Oregon Municipal Finance Officer Association President