August 13, 2015

David Bean
Director of Research
Project No. 3-29E
Governmental Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Dear Mr. Bean:

On behalf of the Tennessee Department of Audit, we thank the GASB for the opportunity to comment on its proposed Exposure Draft (ED), Accounting and Financial Reporting for Certain External Investment Pools. We generally agree with the ED proposals. In addition, we offer the following suggestions for clarifying the ED guidance:

1. For ¶8, consider adding a reference to ¶40 for the definition of shadow pricing since this is the first time the concept is mentioned.

2. Paragraphs 12 and 13 do not necessarily address external investment pools where the weighted average maturity (WAM) and weighted average life (WAL) are the same because of the absence of maturity shortening features (e.g., demand features or interest rate resets). The Tennessee State Pooled Investment Fund (SPIF) administered by the TN Treasury Department does not have any maturity shortening features so the WAM of the SPIF is the same as the WAL. If the ED is issued as presented, the SPIF would not meet the requirements as they are currently operating. After discussion with the Assistant Chief Investment Officer for the SPIF (Cash Manager), the plan of the SPIF would be to continue to operate like a 2a-7 pool and maintain the stable dollar for the fund (stable net asset value per share). In order to do this, the fund would no longer be able to utilize as many investments near the 397 day maturity. We believe this will limit the amount of longer term investments in favor of shorter term investments, which will reduce investment earnings. Another option would be to invest in floating interest rates (which are not as liquid as the U.S. Government securities or Treasuries in which Treasury currently invests). We have been told that there are limits on availability for floating interest rate investments, and it takes longer for a broker to find a buyer. The floating interest rate investments will reduce liquidity of the SPIF, which is one of the fundamental objectives of the fund. We believe the SPIF is a highly liquid fund which currently invests in safe, low risk securities. However, this proposed GASB statement (as presented) may force the TN Treasury Department into buying investments that put additional risk into the fund. In ¶B8, it states that “the specific criteria developed in this Statement to determine if an
external investment pool qualifies for the exception to fair value measurement are organized to address four risks: interest rate, credit, concentration, and liquidity.” We believe the board’s intent was to lower risk; but for this situation, we believe the risk is being unnecessarily increased. Thus, we recommend that wording be included for funds whose WAM and WAL are the same.

3. For ¶20b, we recommend clarifying the sentence to state, “If a security has been rated by more than two NRSROs, without category conflicts, the security….”

4. For ¶23, should “guarantee” in the first sentence be labelled as “non-exchange financial guarantee?”

5. For ¶33, “foreseeable” without context might be too broad to provide meaningful guidance. If the SEC 2a7 rules provide clarity, consider including such timeframe guidance.

6. For ¶34, 35, and 37, the ED limits acquisition of illiquid investments beyond a certain percentage, but what if subsequent transactions (not directly involving illiquid investments) render the investment in illiquid investments higher than 95%? Is there a grace period to get back into compliance? Same for the daily illiquid and weekly illiquid requirements.

7. For ¶38(c), does “agency” include implicitly backed GSEs?

Should you have questions or need clarification on any of our comments, please contact Gerry Boaz or me at (615) 747-5262.

Sincerely,

Deborah V. Loveless, CPA
Director, Division of State Audit