



September 23, 2013

David Bean, Director of Research and Technical Activities

Project No. 26-5P

Governmental Accounting Standards Board

401 Merritt 7, P.O. Box 5116

Norwalk, CT 06856-5116

**RE: GASB Preliminary Views – *Fair Value Measurement and Application***

Dear Mr. Bean:

We appreciate the opportunity to respond to the GASB's Preliminary Views (PV) on *Measurement of Elements of Financial Statements*. Our responses to the Board's questions and additional comments follow.

***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?*

Yes. We agree that the sale of the asset or liability would be considered a hypothetical transaction at the measurement date and that this should be an orderly transaction between market participants and not a forced transaction because in a forced transaction the government is at a disadvantage and likely willing to accept a lesser amount in exchange for the asset or liability.

We cannot locate a definition of "measurement date" throughout the PV. We assume the Board's intent is that the measurement date would be the end of the fiscal year (i.e. June 30), as paragraph 13 of the GASB's Exposure Draft (ED) *Measurement of Elements of Financial Statements* defines the remeasured amounts to be the value at the end of the reporting period. Is it the Board's intent to limit this to fiscal year-end or could other dates be appropriate? In addition to defining measurement date in the body of the document, it would be valuable to include the definition in the glossary.

***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?*

Yes. We agree that transaction costs associated with the sale of an investment should be expensed in the fiscal year of the transaction. We also agree that guidance for investments by defined benefit pension plans and other postemployment benefit plans should be revised to no longer require the inclusion of "brokerage commissions and other costs normally incurred in a sale, if determinable," in

the fair value of the investments. We support the consistent use of fair value measurements regardless of the type of entity involved.

**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?*

Yes, we agree with the Board’s definition of an investment. Additionally, the examples of the application of the definition of an investment include in chapter 3, paragraphs 5 – 13 are quite helpful!

Chapter 3, paragraph 4 states, “an investment asset’s service capacity also may be achieved without generating cash, such as when an investment asset is surrendered to procure services directly in an exchange transaction.” We suggest that the Board provide an example of this type of situation.

**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?*

Yes, we agree with the Board’s view that investments generally should be measured at fair value. Additionally, we appreciate the inclusion of the specific exceptions to this rule within the body of the document.

**Issue 5 – Disclosures:** *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 agree that there is a vast diversity of assets and liabilities that may be measured at fair value and the facts and circumstances unique to each government and therefore it would be impractical to specify criteria for the level of detail in the required disclosures.

The required disclosures are quite lengthy and involved; it would be quite valuable if the Board would include example disclosures for non-financial assets and liabilities (in addition to the investment examples already provided) measured at fair value.

*What other disclosures related to fair value should the Board consider? Why?*

We are not aware of any additional disclosures the Board should consider.

**Additional comments and questions:**

- Chapter 1, paragraph 2 states the scope of the project includes, assets and liabilities already measured at fair value and investments that previously have not been measured at fair value. Chapter 3, Application of Fair Value to Assets and Liabilities, discusses in great detail the definition an investment, provides examples of the application of the definition of an investment and even identifies eleven GASB statements that specifically address measurement of investments that would be impacted by this PV. Chapter 3 does not address liabilities at all, let alone reference any liabilities already measured at fair

value. It is difficult to predict all categories of liabilities the Board may be thinking of without having a complete listing. (Chapter 1, paragraph 9 states that a 2010 survey of preparers included a list of assets and liabilities measured at fair value under existing GASB standards.) We would recommend providing a listing of all prior GASB standards requiring the measurement of liabilities (and assets) at fair value that the Board intends for this PV to impact and example disclosures of fair value information for liabilities. For example, we don't believe the Board is referring to pollution remediation liabilities as these are measured at the "current value" using the "expected cash flow technique" (GASB 49, paragraph 10) or to compensated absences which is "calculated based on the pay or salary rates in effect at the balance sheet date" (GASB 16, paragraph 10).

- Chapter 2, paragraphs 25-27 discuss identifying transactions that are not orderly. Much of the language in these paragraphs is written as if a transaction has actually taken place. For example, paragraph 27 states, "A government would be presumed to have sufficient information to determine whether a transaction is orderly if it is a party to the transaction." This is a bit confusing because as Chapter 2, paragraph 5 states, "The sale of an asset or the transfer of a liability would be a *hypothetical* transaction at the measurement date...Therefore, the objective of a fair value measurement would be to determine the price that would be received for the asset or paid to transfer the liability at the measurement date – that is, an exit price." How can the government be *presumed* to have sufficient information to determine if a *hypothetical* transaction is orderly?
- Chapter 2, paragraph 38 defines Level 3 inputs. We understand that Level 3 inputs are considered unobservable inputs and would be used only when Level 1 and Level 2 inputs are not available. But the following statements could use clarification: (1) although a government may begin with its own data, those data would be adjusted if market participants would do so, and (2) Level 3 inputs would include adjustments for risk when market participants would make such adjustments. These two statements are so broad and not really defined. How do we know when market participants would make adjustments and what type of adjustments? Providing examples and clarification would be beneficial.
- Chapter 2, paragraph 39 defines using quoted prices provided by third parties, however, it does not identify the input level. Is this because it can be Level 1, Level 2 or Level 3? Because this is a required disclosure in the financial statements, we recommend the Board include the input level(s) in the standard.
- Chapter 2, paragraph 45 addresses measurement of liabilities and states "the price paid to transfer the liability to a market participant would be a better measure of fair value than the amount needed to settle with the counterparty." It doesn't seem like there would be a common, or frequent, sale of similar liabilities by governments that would allow for measuring the fair value based on an active market (Level 1 inputs) or quoted prices for similar liabilities or market-corroborated observable inputs (Level 2 inputs). Therefore, it would seem the amount to settle the liability with the counterparty would be more appropriate. Could the Board provide more guidance in this area to assist financial statement preparers in measuring the fair value of liabilities based on the price that would be paid to transfer liabilities to market participants?
- Chapter 2, paragraph 48 discusses restrictions preventing the transfer of a liability. If there are restrictions that prevent a government from transferring its liabilities, why would you even consider

measuring the liability at fair value? What would be the point if there is not a means for disposing of the liability without satisfying the obligation through payments?

- Chapter 3, paragraph 23 – 24 provides changes to existing fair value guidance. Specifically stating items previously measured at fair value should be replaced by acquisition value for capital assets in a nonexchange transaction, donated capital assets, donated works for art, historical treasures, and similar assets, capital assets received in a service concession arrangement, and nonmonetary assets acquired in an exchange when the value of the asset received is used to measure the cost of the asset acquired. We would suggest that the Board provide additional guidance regarding these assets previously reported at fair value which would now be reported at acquisition value. Do these assets need to be restated at acquisition value retroactively to prior periods along with related depreciation, etc.? Is this a change in accounting estimate?

If you have questions or need additional information regarding this response, please do not hesitate to contact Kim Knight at (515) 281-6523.

Sincerely,

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