



August 15, 2014

Mr. David R. Bean
Director of Research and Technical Activities
Project No. 26-5E
Governmental Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Dear Mr. Bean:

The American Institute of Certified Public Accountants (AICPA) has reviewed the Governmental Accounting Standards Board (GASB) Exposure Draft (ED), *Fair Value Measurement and Application*, and is pleased to offer its comments. We appreciate that many of our comments on the related Preliminary Views (PV) document were addressed in the ED. We also continue to support the Board's efforts to address the issues associated with measurement and application of fair value and appreciate the general alignment to the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 820, *Fair Value Measurement*. While we support many of the provisions of the ED, we have a significant concern with the proposed effective date and strongly encourage the Board to defer the effective date by one year to allow governments more time to prepare. Our concern about the effective date and our other significant comments are described in the following section of this letter. We have included our other comments and observations on the ED in the section of this letter titled, "Other Comments."

We would also like to take this opportunity to express our significant concern to the Board regarding the timing of this ED, along with three other significant exposure documents addressing other postemployment benefits and pension non-trust matters. Based on the complexity of these various due process documents, we believe the Board has provided an exceptionally short comment period during a timeframe that is challenging for many preparers and auditors. Our goal is to provide GASB with high quality feedback that reflects our members' views and ultimately helps the Board issue high quality standards. Providing such feedback on topics such as other postemployment benefits in less than 90 days, at the same time we are asked to comment on a complex fair value topic, has resulted in our having to evaluate whether we will be in a position to comment on all of the remaining exposure documents or, alternatively, submit our comments past the formal deadline. We strongly recommend the Board consider extending the comment deadline on one or more of the remaining exposure documents to ensure that our organization, and others, are in a position to provide GASB with the high quality feedback it needs for future deliberations on these important topics.

SIGNIFICANT CONCERNS

Effective Date and Transition Guidance Should be Amended. The proposed effective date of this Statement is for periods beginning after June 15, 2015. With the final Statement expected in February 2015, governments would have just over one year to implement it. Based on the experiences of the private sector in implementing FASB's fair value standard, we believe the proposed GASB timeframe will not be sufficient. It is our understanding that the private sector had over two years of lead time to implement the FASB standard and that many still had difficulty meeting the effective date timeframe. Adding to the implementation challenge for the governmental sector are the large public employee retirement systems and investment trusts that have thousands of securities. These entities and trusts will have to develop processes to evaluate the inputs as they cannot solely rely on custodians or service providers to determine the classification of each investment as Level 1, 2, or 3 and related disclosures. While applying the fair value provisions of the ED to marketable equity securities will be relatively straight-forward, the application to certain fixed income investments and alternative investments will be significantly more challenging and time consuming. Therefore, we strongly recommend the Board change the effective date to periods beginning after June 15, 2016.

In addition to delaying the effective date, we strongly encourage the Board to revise its proposed transition requirements. We recommend a transition provision that is on a prospective basis with certain exceptions. In the related FASB standard, the transition was generally prospective for presentation and disclosures, but for certain transactions, the FASB required a "modified retrospective" approach (that is, upon adoption a cumulative-effect adjustment was recorded to the opening balance of retained earnings). We recommend the GASB include a similar transition provision as we believe the benefit of GASB's proposed full retrospective restatement will not outweigh the related costs. Additionally, we strongly question the benefit of requiring governments to prepare all of the required disclosures for prior periods and recommend that the final Statement be clear that the disclosures are prospective (that is, for the period of implementation and into the future).

Separate the Measurement and Application Aspects into Two Statements. As we proposed in our response to the PV, we continue to recommend the Board separate the measurement and application aspects of the fair value project and create two Statements. The ED continues to be confusing to follow as the measurement discussion is more conceptual and applies broadly, whereas the application section narrows the focus to investments. Separating the two aspects would more effectively facilitate applying fair value to transactions other than investments in the future.

Permit Settlement Value for Certain Interest Rate Swaps. We encourage the Board to provide a practical expedient that allows governments to use settlement value in proxy of fair value for interest rate swaps. Interest rate swaps are over-the-counter instruments that typically follow the standard International Swaps and Derivatives Association or ISDA swap agreement. These instruments are non-transferable and cannot be traded in the

secondary market. Additionally, they can only settle prior to the maturity (expiration) based on the settlement provisions within the agreement (which are typically based on the present value of payment streams exclusive of the credit risk of either party). It also seems counterintuitive for a government to recognize a gain (or reduction of a liability) for their own decline in credit rating, especially when this gain may not be realized through sale or transfer of the swap. Since settlement value is predominantly used in practice today for these instruments, the proposal to change to fair value will be significant and costly. Thus, we question the proposed requirement to present such interest rate swaps at fair value as settlement value is generally easier to determine while also providing decision-useful information to users.

Change of Accounting for Fixed Income Investments Held to Maturity. We suggest the Board require that changes in the fair value of fixed income investments held to maturity be reported as either deferred outflows of resources or deferred inflows of resources in the statement of net position. This accounting treatment would best address interperiod equity and may address some of issues related to the "matchbox concept" raised in responses to the PV.

Clarify Prohibition of Blockage Factor. The Board clearly prohibited the use of a blockage factor for Level 1 measurements in paragraph 38, but the ED is silent as to blockage factor use for Level 2 and Level 3 measurements. We believe prohibiting a blockage factor for all levels is a better conceptual answer since regardless of level (for a given unit of account) the measurement should not reflect the ability of the holder of the investment to potentially sell it all at once when it could be sold in smaller increments for a higher amount. Such a prohibition would likely improve comparability and makes the measurement less subjective since blockage factors are not likely to be observable inputs.

Further, we also suggest the Board define the term "blockage factor" in the glossary to the final Statement. While paragraph B22 of the ED's Basis for Conclusions includes a definition, it will be excluded when the final Statement is codified.

OTHER COMMENTS

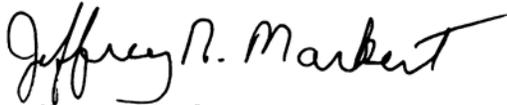
Provide Examples of Changes in Valuation Techniques That are More Applicable. There are two examples in the ED (paragraphs 48 and 78.a.4) that illustrate a change in valuation technique. In both of these examples the relief from royalty technique is part of the example. We believe the relief from royalty technique would be used very infrequently by governments and recommend that the Board provide more applicable examples. In addition, we noted that the techniques cited in the examples are not all defined terms and would suggest alternate phrasing. For example, we suggest that paragraph 48 be revised to state, "for example, changing from a technique using market multiples to a present value technique." Further, we suggest paragraph 78.a.4 be revised to state, "for example, changing from a technique using expected cash flows to a technique using market multiples or the use of an additional valuation technique." If the Board makes these suggested changes, the Board should consider whether the phrase "relief from royalty technique" should be maintained in the glossary. If maintained, we noted that the term "relief from

royalty method” is defined in the AICPA *Professional Standards*, in Statement on Standard for Valuation Services No. 1 (SSVS No. 1), *Valuation of a Business, Business Ownership Interest, Security, or Intangible Asset*. We encourage the Board to consider this definition as consistency in terms and definitions across the GASB and AICPA literature is preferable where possible.

Level 3 Disclosure on Effect of Investment Income Should be Eliminated. We recommend the Board eliminate the disclosure requirement in paragraph 78.a.5 because it appears to be solely related to the Level 3 rollforward which was a concept in the PV that was deleted in the ED.

The AICPA appreciates the opportunity to comment on the ED. This comment letter was prepared by members of the AICPA’s State and Local Government Expert Panel and was reviewed by representatives of the Financial Reporting Executive Committee who did not object to its issuance. Representatives of the AICPA would be pleased to discuss these comments with you at your convenience.

Sincerely,



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Chair
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Expert Panel



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cc: State and Local Government Expert Panel
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