

November 11, 2008

Mr. David R. Bean
Director of Research and Technical Activities, Project Nos. 33 and 33-1
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 Drafts (EDs), *Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards* and *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, and is pleased to offer its comments. We fully support the GASB's efforts to incorporate both the accounting principles and the hierarchy of generally accepted accounting principles (GAAP), originally covered in the AICPA's auditing literature, into the GASB's accounting and financial reporting standards.

We agree with the Board's conclusion that the migration of these standards into GAAP for state and local governments will improve financial reporting by making available in a single place all sources of GAAP. It will also allow the Board to modify the guidance, as necessary, to appropriately recognize the governmental environment and the needs of governmental financial statement users.

As noted in the Appendix to this letter, we are recommending several changes to the proposals in areas we believe need additional clarification or explanation to appropriately address the governmental environment. The most significant recommendations relate to the discussion of subsequent events and going concern considerations in the ED titled, *Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards*.

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

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Sincerely,



Frank W. Crawford
Chair
AICPA State and Local Government
Expert Panel



Mary M. Foelster
Director
AICPA Governmental Auditing
and Accounting

cc: State and Local Government Expert Panel
Jay D. Hanson
Daniel J. Noll
Charles E. Landes

APPENDIX—COMMENTS AND RECOMMENDATIONS

Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards

Clarification Needed Regarding Source of Related Party Transactions Disclosure Requirements. Footnote 1 to paragraph 4 of the ED discusses the sources for related party disclosure requirements which include Financial Accounting Standards Board (FASB) Statement No. 57, *Related Party Disclosures*. The parenthetical reference in the footnote indicates that FASB Statement No. 57 is only applicable to governmental entities to the extent the guidance does not conflict with or contradict GASB pronouncements. We recommend that the GASB clarify where there are conflicts or contradictions between FASB Statement No. 57 and GASB pronouncements to promote consistency in related party disclosures.

Routine Transactions and Related Party Considerations. Paragraph 7 of the ED states that, except for routine transactions, it may not be possible to determine whether a transaction would have taken place or what the terms and conditions would have been had the parties not been related. We believe that even in routine transactions it may not be possible to make these determinations. Therefore, we suggest deleting the phrase “Except in routine transactions” from the opening sentence in paragraph 7.

Descriptive Terminology for Subsequent Events Would Improve Understanding. We have found that the terms “Type one” and “Type two” subsequent events have caused confusion in practice. Therefore, we recommend the Board take this opportunity to adopt more descriptive terminology to improve understanding by financial statement preparers and other users. Recently, the FASB in its ED titled, *Subsequent Events*, has proposed replacing the confusing “Type one” and “Type two” terminology with the terms “Recognized” and “Unrecognized.” We encourage the Board to consider adopting a similar approach to improve the understanding of subsequent events terminology going forward.

Criteria Reference Needed for Correction of an Error and Prior Period Adjustment. Paragraph 14 of the ED states that events occurring between the time of original issuance and reissuance of the financial statements should not result in adjustment of the financial statements unless the adjustment *meets the criteria for the correction of an error or the criteria for prior-period adjustments*. AU section 560.08 currently refers to Opinions of the Accounting Principles Board and FASB Statement No. 16, *Prior Period Adjustments*, as the source of the criteria. The ED does not carry forward these references. We recommend that since the ED refers to the criteria relating to a correction of an error or prior period adjustment that specific references to the literature containing the relevant criteria be added. This will improve the utility of the final standard to both preparers and other users.

Subsequent Events Section Could be Improved With Additional Example. Paragraph 12 of the ED discusses subsequent events affecting the realization of assets or the settlement of estimated liabilities. For clarity, we recommend that this paragraph be modified to include an example to further illustrate this concept (similar to the example associated with paragraph 6 of the ED on the substance of arms length transactions). GASB Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*, paragraph 18, discusses the treatment of sales of receivables with recourse obligations or provisions. We suggest that this example, or a similar example, be included to illustrate the concept in paragraph 12 of the ED.

More Detail Needed About the Level that Preparers are Required to Make the Going Concern Assessment. Given the unique reporting structure of governmental entities (that is, required reporting units defined by GASB), we suggest that the final standard specify the level at which governments should assess the ability to continue as a going concern. The ED is silent as to whether preparers are required to make the going concern evaluation at the entity level or at the individual reporting unit level. As noted in the Board's reasoning for taking on this project, moving the going concern guidance from the auditing literature to the accounting literature provides the Board with the opportunity to modify the guidance, as necessary, to appropriately recognize the governmental environment and the needs of governmental financial statement users. This is an area that needs such modification.

Although we recognize that AU section 341 has not previously addressed this issue from a preparer's perspective, paragraph 13.15 of the AICPA Audit and Accounting Guide, *State and Local Governments*, does address this matter from an auditing perspective. It states the following, "In a governmental audit, the auditor should make the going concern evaluation for the entity as a whole, not for individual opinion units." We recommend that the Board take this opportunity to modify the guidance that has previously existed and to clearly state that the going concern assessment should occur for state and local governments at the entity level. Such clarification will assist preparers in appropriately applying the standard and will also assist auditors in defining their reporting responsibilities.

Going Concern Discussion May Lead to the Erroneous Conclusion that a Going Concern Not Possible for State and Local Governments. As stated in the ED, we agree with the premise that the continuation of an entity as a going concern is assumed in the absence of significant information to the contrary. However, we believe the discussion of the government environment in paragraph 17 of the ED, provides so much flexibility for governments that they may mistakenly believe that a going concern conclusion is not possible in any case. We understand the Board's intention to describe the unique environment of governmental entities, but think that it may mistakenly create a presumptive criteria that a government is unlikely to go bankrupt or have going concern issues. We suggest, at a minimum, including a statement in paragraph 17 that a going concern situation is possible and has occurred for some state and local governments.

Disclosures When Substantial Doubt Exists, but was Alleviated. We noted that AU section 341.11 was not carried forward into the proposed standard for preparers. It included the following:

“When, primarily because of the auditor’s consideration of management’s plans, he concludes that substantial doubt about the entity’s ability to continue as a going concern for a reasonable period of time is alleviated, he should consider the need for disclosure of the principal conditions and events that initially caused him to believe there was substantial doubt. The auditor’s consideration of the disclosure should include the possible effects of such conditions and events, and any mitigating factors, including management’s plans.”

We were unclear why the Board did not carry forward a similar disclosure concept for preparers that would require a government to disclose the principal conditions and events that initially caused the substantial doubt leading to the going concern evaluation. This is particularly important in a government environment in that, as paragraph 17 points out, there are few going disclosures actually made in the state and local government environment due to the many factors that may diminish the possibility of a going concern. While we recognize that some of the information intended by AU section 341.11 may be discussed in the management’s discussion and analysis, we believe that the current practice of requiring such disclosure in the footnotes should be continued.

Editorial Changes Needed in Paragraphs 5 and 11. The discussion in paragraphs 4 through 7 of the ED highlights the importance of considering the substance of transactions rather than the legal form when related party transactions occur. Paragraph 5 of the ED appears to be intended to provide examples of transactions where substance would be important in a related party scenario. However, the sentence that precedes the bulleted transaction listing uses the term *form-over-substance*. We believe the Board intended to use the term *substance-over-form* in paragraph 5 and recommend that the term *form-over-substance* be replaced by *substance-over-form*. Additionally, we believe there is another editorial change needed in paragraph 11. The second sentence of that paragraph refers to a “major water utility customer’s deteriorating financial condition.” We believe that the Board intends this sentence to refer to an entity’s “major customer” instead of the utility itself being major. Therefore, we recommend that the second sentence be revised to read as follows: “...a water utility’s major customer having deteriorating financial condition...”

FASB Exposure Drafts Titled, Subsequent Events and Going Concern. One development that has occurred since the GASB issued its EDs is the issuance of two similar exposure drafts by the FASB titled, *Subsequent Events*, and *Going Concern*. The FASB, like the GASB, is moving these accounting concepts into its own literature. However, we would like to bring to your attention that if FASB standards are finalized in their current form, there will be some differences between FASB and GASB guidance because the FASB is also attempting to align its guidance with the International Financial Reporting Standards. For example, the FASB would require preparers to disclose the date through which subsequent events were considered while GASB standards would not impose such a requirement. Also, the FASB is proposing that the time horizon for the assessment of the going concern assumption be expanded to the period of *at*

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least, but not limited to twelve months from the end of the reporting period while the GASB standards would require evaluation for a period *not to exceed* one year beyond the date of the financial statements. The GASB may want to consider the FASB proposals to determine whether any aspects of those proposals would also be appropriate in a state and local government environment.

***The Hierarchy of Generally Accepted Accounting Principles
for State and Local Governments***

Other Accounting Literature. Paragraph 6 provides examples of *other accounting literature*. The list did not include consensus positions of the FASB Emerging Issues Task Force and AICPA Practice Bulletins. While these two items can be inferred as incorporated based on the relevance and specificity, it may be beneficial to specifically include them in the list of examples.