



August 15, 2014

Mr. David Bean  
Director of Research and Technical Activities  
Governmental Accounting Standards Board  
401 Merritt 7  
PO Box 5116  
Norwalk, Connecticut 06856-5116

Re: Project No. 26-5E

Dear Dave:

On behalf of the National Association of College and University Business Officers (NACUBO), we submit the following comments on the Exposure Draft (ED) of the Governmental Accounting Standards Board (GASB), "Fair Value Measurement and Application." NACUBO's comments on the ED were developed with input from member institutions and our Accounting Principles Council (APC). The APC is comprised of experienced business officers from both independent and public colleges and universities.

NACUBO is a nonprofit professional organization representing chief financial and administrative officers at approximately 2,500 colleges and universities. In its capacity as a professional association, NACUBO develops accounting and reporting guidance for the higher education community and offers professional development for college administrative professionals on a wide array of financial management and reporting topics.

We are pleased that the Board is examining assets and liabilities currently measured at fair value and addressing alternative investments that previously have not been measured at fair value. These kinds of investments are a significant component of many colleges and universities endowments. Respondents to the 2013 annual NACUBO-Commonfund Study of Endowments collectively managed \$447 billion of investments of which 55 percent were invested in alternative strategies. Further, the alternative investment allocation for public universities (not including affiliated not-for-profit foundations) in 2013 was 52 percent.

Alternative investments do not have a readily determinable market price and there is no current guidance for valuing or explaining these assets in GASB's literature. We value the Board's efforts in reviewing the work of the Financial Accounting Standards Board (FASB) on fair value measurement and are grateful for the opportunity to offer our comments. Our comments are in ED paragraph numeric order.

Unit of Account (paragraphs 7 and 8):

Paragraph 7 states that a particular asset or liability measured at fair value might be a stand-alone asset or liability, a group of assets, a group of liabilities, or a group of related assets and liabilities. However, paragraph 8 does little to place this statement in context, especially for the complicated structures that are commonly used in alternative investments.

While paragraph 8 defines unit of account in a manner that is similar to the definition in FASB's master glossary, the definition appears to blur the lines between measurement, recognition, and reporting. We suggest clarification of the term "as provided in the accounting standards" because there is no specific codified accounting guidance for reference. We also recommend the addition [or inclusion] of an explanation of the difference between unit of account measurement and what the reporting entity should recognize. To illustrate, please review the following suggested revisions (*emphasized*):

8. Recognition or disclosure of an asset or liability—whether a single asset or liability, a group of assets, a group of liabilities, or a group of related assets and liabilities—depends on the **unit of account** of the asset or liability. The unit of account refers to the level at which an asset or a liability is aggregated or disaggregated for recognition purposes as provided by the accounting standards (*include a citation example or a separate paragraph that illustrates or explains applicable accounting standards, or delete the phrase "as provided by the accounting standards" – the glossary does not include the phrase.*). *The unit of account's valuation* will vary depending on the measurement attribute applied. The measurement attributes are historical cost, fair value, replacement cost, and settlement value. *Once the unit of account is established*—whether at an individual item level or an aggregated level—*recognition and disclosure by the governmental reporting entity is based upon the reporting entity's ownership interest (e.g., the entire asset or liability, shares, or percentage).*

Even if the Board chooses not to address ownership interest in paragraph 8, we strongly recommend expanding the examples in Appendix C to address a limited partnership investment. In a limited partnership investment, the reporting entity owns an "interest" or percentage of the investments held by the partnership. Each individual investment is owned by the partnership and the limited partners own a share of that partnership rather than a share of each individual investment. For the majority of alternative investments, the appropriate recognition consideration for the reporting entity is the interest in the investee fund itself, not the underlying investments held by the fund. This is because the reporting entity owns an undivided interest in the whole of the investee fund portfolio and typically lacks the ability to dispose of individual assets and liabilities in the investee fund portfolio. The limited partnership structure is quite common among colleges and universities with alternative investments in their endowment pool.

Paragraph 14 – Markets:

“Even if there is no observable market to provide pricing information about the sale of an asset or the transfer of a liability at the measurement date, a fair value measurement should assume that a transaction takes place at that date, **considered from the perspective of a market participant that controls the resource or is obligated for the liability**. That assumed transaction establishes a basis for determining the price to sell the asset or to transfer the liability.”

The wording in paragraph 14 (bold font above) of the draft is potentially confusing. The above wording reads as if the price, and consequently fair value, is determined by the seller when no market exists (because the seller controls the asset or is obligated for the liability). This perspective is inconsistent with the definition of fair value in the glossary and paragraph 5: “fair value would be the amount received to sell an asset or paid to transfer a liability in an orderly transaction between market participants.” Although buyers and sellers are market participants, when an asset is sold or a liability is transferred, the price is the amount that a buyer will pay (and the seller will receive). We offer the following wording:

“Even if there is no observable market to provide pricing information about the sale of an asset or the transfer of a liability at the measurement date, a fair value measurement should assume that a transaction takes place on that date. The assumed transaction establishes a basis for determining the price that a buyer is willing to pay and a seller is willing to accept.”

Paragraphs 37 and 41 – Adjustments to Level 1 and 2 inputs, respectively:

It would be helpful if the wording in these paragraphs made it clear from the beginning that an adjustment to these inputs would result in the asset no longer being classified in that level. For example, although circumstances are listed in which adjustments could be made to Level 1 inputs, once an adjustment is made to a Level 1 input, it becomes a Level 2 or Level 3 input.

Disclosures:

Paragraph 78a (5) – “For fair value measurements categorized in Level 3, other than those that calculate NAV per share or its equivalent, the effect of those investments on investment income for the reporting period.” We believe that this sentence was inadvertently retained from the Preliminary Views (PV) document when the requirement for a Level 3 roll-forward was eliminated in the ED. If that is not the case, an explanation of the reason for the disclosure would be helpful. If it is meant to be a required disclosure and a government has a significant number of these investments, it could be difficult to obtain the information.

Paragraph 79c – It is unclear why unfunded commitments must be disclosed only for investments for which NAV is calculated. We would expect that disclosure of information about all unfunded commitments would be required.

When comparing disclosures required by FASB per ASC 825-10-50-6A with the requirements proposed in paragraph 79, we noticed that the ED uses the word “type” where FASB uses the word “class” for the same disclosure requirements. Paragraph 77 of the ED states that “disclosures required by this Statement should be organized by type or class of asset or liability,” and subparagraph (b) implies that there is a difference between type and class as follows:

*“The level of the fair value hierarchy within which the fair value measurement is categorized. A greater degree of uncertainty and subjectivity suggests that the number of types and classes may need to be greater for fair value measurements categorized within Level 3 of the fair value hierarchy.”*

It is unclear to us what distinction the Board is attempting to make by using the terms type and class. We recommend that the ED use only “class,” rather than “type,” or if both terms are retained, that definitions for “type” and “class” be added to the glossary. As written, we are concerned that perceived differences between type and class may lead to more disaggregation of disclosures by public institutions and other governmental reporting entities compared with reporting entities that follow FASB.

In addition, FASB ASC 820-10-50 (Fair Value Measurement Disclosures) clearly uses the same wording as paragraph 77, subparagraph b of the ED but augments subparagraph b as follows (**emphasis added**):

*“The number of classes may need to be greater for fair value measurements categorized within Level 3 of the fair value hierarchy because those measurements have a greater degree of uncertainty and subjectivity. **Determining appropriate classes of assets and liabilities for which disclosures about fair value measurements should be provided requires judgment.**” (ASC 820-10-50-2b)*

Based upon experiences of colleges and universities that follow FASB guidance, judgment and flexibility is essential when dealing with the diverse investment classes and configurations among alternative investments that are categorized within Level 3 of the fair value hierarchy. We respectfully request that GASB defer to the experience of the FASB and its preparers by including the above language (from ASC-10-50-2b) in paragraph 77.

Regarding the need for judgment, we are concerned with the level of detail provided in the illustrative disclosure on page 60. We note that a similar disclosure example in FASB ASC 820-10-55-100 includes footnotes clarifying the reporting entity’s decision around the level of aggregation or disaggregation within the disclosure based on the nature, characteristics, and risks of the investments. We believe that adding similar footnotes to the sample disclosure in the ED would acknowledge that there is judgment and, therefore, flexibility in the level of detail provided based on the reporting entity’s specific holdings in a given investment.

Finally, related to the above points, a public university system that participated in the field test of the guidance included in the PV on fair value measurement noted that the detail required for Level 3 disclosures was so prescriptive that it would add up to six additional pages of notes. That level of disclosure exceeds FASB's requirements. We believe this is a significant point, given that both standard setting bodies are considering how to best address disclosure volume.

Effective Date:

We are concerned that the proposed effective date of periods beginning after June 15, 2015, provides insufficient time for preparers to implement the standard. We have learned from higher education institutions that follow FASB guidance that a significant amount of time is required for implementation—especially for those that have a large number of alternative investments. Proper leveling of investments within the fair value hierarchy requires assessing each one. This means reviewing the terms of each investment, documenting the methodology used by third parties to estimate fair value, and understanding any limitations on redemption. While investment brokers and custodians have developed reports that provide the leveling information for investments that they manage, those reports are really just a starting point and cannot be relied upon for audit purposes. Because of the many nuances that exist between Level 2 and Level 3 investments, third-party reports are not entirely accurate as they use a broad approach to leveling. For example, they may include all debt investments in Level 2 when, in fact, the inputs used by a third-party pricing service may more appropriately be considered Level 3 inputs.

Many large institutions have thousands of individual investments, and the amount of time required to prepare for implementation is considerable. In addition, given the complexity of the proposed standard, implementation guidance will be critical. Considering anticipated requirements for due process surrounding implementation guidance, however, we question whether the proposed effective date allows the Board and staff sufficient time. We strongly urge the Board to postpone the effective date for one year – for periods beginning after June 15, 2016.

We wish to express our appreciation for the opportunity to comment. We look forward to answering any questions the Board or the staff may have. Please contact me at 202-861-2542 or [sue.menditto@nacubo.org](mailto:sue.menditto@nacubo.org).

Sincerely,

Susan M. Menditto  
Director, Accounting Policy