



**Public Pension Financial Forum
c/o Ohio Public Employee Retirement System**

277 East Town Street

Columbus, Ohio 43215-4642

September 30, 2013

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

Subject: Project No. 26-5P

Dear Board and Staff:

The Public Pension Financial Forum (P2F2) is pleased to have the opportunity to respond to the Government Accounting Standards Board (GASB) Project No. 26-5P, Preliminary Views (PV) document on "Fair Value Measurement and Application."

P2F2 was formed in 2004. The purpose of this organization is to promote excellence in public pension plan financial operations, provide educational programs of current interest to the membership, promote the exchange of ideas concerning financial operations and reporting between public pension plans, and to foster sound principles, procedures and practices in the field of public pensions related to the financial operations of such plans. Membership is open to any finance employee of a public pension who supports the purposes of P2F2. The organization currently has 201 members representing 100 plans, offering defined benefit, defined contribution and hybrid plans.

We would like to thank GASB for considering changes to the Fair Value Measurement and Application PV. We are in general agreement with the pension plan financial reporting PV. However, we do have several issues of concern.

As requested, attached are responses to the Board's specific questions on page viii in the PV.

Issue – 1: Definition of Fair Value

We agree with the Board’s preliminary view on the definition of fair value. We feel that users of financial statements would benefit if GASB’s definition of fair value is consistent with the definition used in other standards (e.g., FASB 157/ACS 820).

Assets owned by most governmental pension funds are priced by an independent third-party pricing service and a definition consistent with FASB allows us to continue using these services. In addition, these services currently price assets owned by non-governmental pension funds (e.g., corporate plans, foundations, and endowments) and an inconsistent definition, in our view, would present a challenge to the pricing services, and increase administrative costs to governmental plan sponsors.

Issue – 2: Transaction Costs

We agree with the Board’s preliminary view on treating transaction costs as period costs, which coincides with current industry practice. Currently, third-party pricing services do not reduce fair value by the expected transaction costs. Government-sponsored funds can execute thousands of transactions and hold thousands of securities in a given reporting period. Any deviation from the current practice would cause undue hardship in maintaining the financial records used to prepare financial statements.

Issue – 3: Definition of an Investment

We agree with the Board’s preliminary view on the definition of an investment.

It is our understanding that this definition includes securities considered to be liabilities and we agree with this aspect of the definition. However, we are concerned about how this will impact the ability to reconcile the Level I, II, III disclosure to the Statement of Net Position since liabilities are not included in the total investment assets. While not part of the PV, we feel liabilities that are an integral part of an investment strategy should be “rolled up” with the investment assets (e.g., a separate portfolio containing long and short equity positions).

Issue – 4: Measurement of Investments

We agree with the Board’s preliminary view that investments generally should be measured at fair value on a recurring basis in accordance with existing literature.

In addition, we agree with the Board’s preliminary view that governments should be permitted to measure investments, that don’t have a determinable fair value, using a practical expedient and measure these investments according to the net asset value (NAV) per share. We feel the Board should include the definition of “practical expedient” in the glossary and clarify the explanation in paragraphs 43 and 44 on page 15 of the PV. The definition found on page x should also be expanded upon.

Issue – 5a: Disclosures

We agree with the Board’s preliminary view that the fair value measurements disclosure shown in Appendix B, Illustration 2 on page 33 should be required. We feel users of financial statements deserve to know what portion of plan investments are valued using reliable valuation techniques and which portion of investment positions are valued using less-reliable valuation techniques. We are also happy to see the Board chose to be consistent with FAS157/ACS 820 and adopt the same criteria surrounding the fair value hierarchy of inputs. This consistency allows government-sponsored plans to follow similar methods that corporate-sponsored plans are using to categorize their investments as Level 1, 2, or 3. This also allows for auditors of these plans to use the same leveling criteria to determine accuracy of this disclosure. However, we have some concerns and request additional guidance about the sample disclosure.

- We agree with the Board’s preliminary view that specific circumstances of a government would dictate the level of disaggregation and the amount of detail to disclosure.
- We question the reasoning behind disaggregating equity securities by industry sector. In practice we have had difficulty determining the correct sector for a number of securities due to the wide range of business a corporate-conglomerate conducts. For example, would the fair value of common stock for General Electric be classified in the financial services or manufacturing sector? We do not feel this classification will be consistently applied by governmental public pension plans.
- We feel it is misleading to present real estate and private equity funds under a category of hedge fund investments and that the disclosure example needs modification.
- We feel it is misleading to present all commercial mortgage-backed securities and collateralized debt obligations as Level 3. Multiple government-sponsored funds have received information from their custodian indicating that Level 2 is the correct classification for all their investments in these categories, based on the underlying inputs used by the third-party pricing vendors to value these securities. We ask the Board to consider changing the disclosure to present the majority of these securities in the Level 2 category.
- We feel it is misleading to present the majority of residential mortgage-backed securities in the Level 3 category. Multiple government-sponsored funds have received information from their custodian indicating that Level 2 is the correct classification for all their investments in this type of security, based on the underlying inputs used by the third-party pricing vendors to value these securities. We ask the Board to consider changing the disclosure to present the majority of these securities in the Level 2 category.

- Regarding investments that calculate a NAV, we ask the Board to clarify that the entire investment be classified as Level 1, 2, or 3 based on the fair value hierarchy criteria. We would like to confirm that preparers do not need to report the level criteria of the allocated portion of the underlying assets within these funds. In other words, the governmental reporting entity is required to determine the level classification on a fund-by-fund basis and not on a basis which considers the level of the individual underlying assets of these investments.

Allocating on a basis using the individual underlying assets is not practical due to (1) the unique nature of how ownership interest can be defined and (2) the many instances where the governmental plan year-end does not coincide with the year-end of the fund. In addition, a number of government funds currently own foreign funds which do not prepare GAAP financial statements making this allocation impossible.

We disagree with the Board's preliminary view that the Quantitative Information about Level 3 Fair Value Measurements in Appendix B, Illustration 2 on page 35 should be required. Below are the reasons we feel this disclosure shouldn't be required for government-sponsored plans.

- As previously mentioned, government-sponsored plans typically own thousands of investments where a subset of these investments meet the Level 3 criteria. Due to the number of investments, government-sponsored plans typically rely on the custodian of the investments to contract with a third-party pricing vendor to provide valuation data. One custodian that we have contacted confirmed that it is "beyond the custodian" to provide information related to the specific unobservable inputs shown in this disclosure or this information would come at a considerable cost. We feel if we are unable to receive this information from a custodian it is not practicable to obtain this information in a cost-effective manner.
- We appreciate that there is no requirement to disclose specific assumptions if the pricing vendor considers those assumptions to be proprietary and, after a government makes a reasonable effort, the pricing service declines to make that information available. In our discussions with one custodian, we learned there are pricing vendors that will not divulge any specifics [even to the custodian who has contracted with that vendor] about some models used to determine valuations of specific security types. We feel that obtaining this information directly from the pricing vendor, with whom many government-sponsored plans have no contract or relationship, is a futile task. We also wonder if this inquiry would need to be made year-after-year only to be told the same answer. At best, this disclosure would only contain information pertaining to a subset of Level 3 investments held by the reporting entity. We feel that presenting this schedule for only a subset of securities could be misleading for users of the financial statements as the ranges presented may not represent the entire population of Level 3 assets.

- Assuming, on a hypothetical basis, that a government-sponsored plan was able to obtain all the required information for all investments, there could be hundreds of assets in each Level 3 category for some benefit plans. The number of assets in this disclosure could be considerably more if mortgage-backed and collateral debt obligations ultimately meet the Level 3 criteria (The information we have received to-date indicates the vast majority of these investments meet the Level 2 criteria).

We feel that FASB's summary of respondents on Statement No. 157 regarding proposed sensitivity disclosures in the Basis for Conclusions (BC17) adequately summarizes our feelings about this schedule for government-sponsored plans. To paraphrase, "the information provided by the disclosures would not be decision useful because the range of reasonable possible Level 3 [unobservable inputs] would be extremely wide and, thus would be meaningless and possibly confusing to users." In our review of financial statement disclosures made by corporate-sponsored benefit plans, we don't see this schedule produced and ask the Board to consider the reasons why this is a unique requirement for government-sponsored plans.

We also disagree with the Board's preliminary view that governments should disclose a narrative description of the sensitivity of fair value measurements to changes in unobservable inputs in the notes to the financial statements about recurring fair value measurements categorized in Level 3 of the fair value hierarchy. In our opinion, it is not possible to prepare these disclosures due to the proprietary nature of the valuation models (discussed previously). We also feel that FASB's summary of respondents on Statement No. 157 also applies to this narrative disclosure (discussed above). We ask the Board to reconsider this requirement for these reasons and also reconsider the need for this disclosure if "In many cases, the Board believes that Statement 40's risk disclosure also would satisfy this Level 3 narrative disclosure requirement" (see paragraph 12, page 24 of the PV).

We agree with the Board's preliminary view that the Fair Value Measurements of Certain Entities that Calculate Net Asset Value per Share shown in Appendix B, Illustration 2 on page 36 should be required. We agree with the Board's preliminary view to exclude redemption frequency for real estate and private equity funds in the disclosure example as this is a complex matter unique to each individual investment in this category. We do not agree with the following aspects of the notes to this disclosure.

- The notes in the example are too detailed and granular when a government-sponsored pension plan can hold hundreds of these investments.
- The requirement to disclose plans to sell a portion of these investments is problematic for a couple of reasons. Secondary sales of real estate and private equity funds are very complex and difficult to complete. The general partner often needs to approve the sale and at the time of this disclosure there is no certainty that the sale will materialize, thus often making this disclosure incorrect after-the-fact. In addition, we feel that disclosing

an entity's plans to sell a number of investments could impact the sales price the entity receives. We feel these potential sales are highly confidential and making these disclosures is a breach of our fiduciary responsibility.

Issue – 5b: Additional Disclosures

We do not think the Board should consider any additional disclosures for government-sponsored plans which are not required by FASB 157/ACS 820. As previously mentioned, we feel users of financial statements deserve to know what portion of the plan investments are valued using reliable valuation techniques and which portion of investment positions are valued using less-reliable valuation techniques. However, we don't feel additional disclosures regarding Level 3 investments offer any value to the financial statement users due to the inherent complexities associated with valuing investments using unobservable inputs. These complexities can be unique to each model, which makes aggregating this information at any level misleading. We feel the proprietary issues also prevent preparers from compiling any sort of additional disclosure on these investments. Any disclosures compiled from a subset of information would possibly be misleading.

We are also concerned about the volume of standards that have been impacting government-sponsored plans recently and the ability of the plans to assimilate all of the changes. This is most concerning for smaller multiple employer plans throughout the country. We feel the Board should consider the timing of any new standard on fair value in light of the additional work that has been placed upon government-sponsored plans by the issuance of GASB 68.

Again, we appreciate the opportunity to comment on this project. Should you have any additional questions regarding these comments, please feel free to contact our organization by emailing Karl Greve at kgreve@copera.org.

This response was prepared by a collective effort of the P2F2 membership. By our e-mail submission, the P2F2 Board of Directors substantially agrees with the views in the form presented in this response. However, there are some areas where one or more P2F2 directors may have a slightly different perspective which will be shared with GASB in their systems' separate responses to the PV.

Sincerely,

A handwritten signature in black ink that reads "Art Hewig". The signature is written in a cursive, slightly slanted style.

Art Hewig

P2F2 President