

## GASB Statement 72

### Fair Value Measurement and Application

## Overview

- **What:** The GASB issued Statement 72 to update the existing standards on fair value (primarily Statement 31)
- **Why:** Review of existing standards found opportunities to improve the measurement of resources available to governments, and to increase comparability and accountability
- **When:** Effective for fiscal years beginning after June 15, 2015

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## Fair Value Definition

- 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.
  - An exit price
- Other characteristics of fair value
  - Market-based
  - Based on a government's principal or most advantageous market
- Fair value is not an option – it is required

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## Valuation Techniques

- Apply valuation technique(s) that best represents fair value in the circumstances
  - **Market approach** – Using prices and other relevant information generated by market transactions involving identical or similar assets or liabilities
  - **Cost approach** – Amount that would be required currently to replace the service capacity of an asset
  - **Income approach** – Converts expected future amounts (for example, cash flows) to a single current amount (that is, discounted)
- Revisions due to a change in valuation technique(s) are considered a change in accounting estimate

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## Inputs

- Maximize use of relevant observable inputs and minimize use of unobservable inputs
- Inputs should be consistent with the characteristics of the asset or liability
- Based on bid and ask prices
- **Level 1:** quoted prices (unadjusted) in active markets for identical assets or liabilities, most reliable
- **Level 2:** quoted prices for similar assets or liabilities, quoted prices for identical or similar assets or liabilities in markets that are not active, or other than quoted prices that are observable
- **Level 3:** unobservable inputs, least reliable

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## Measurement—Net Asset Value Per Share (NAV)

- Measuring fair value of investments in certain entities that calculate net asset value (NAV) per share or its equivalent
- NAV per share may be used as a practical expedient to estimate fair value
  - Adjustment to NAV per share amount may be necessary to be consistent with measurement principles
  - May be applied on an investment-by-investment basis but must be applied consistently to fair value measurement of the government's entire position in a particular investment
- If sale of a portion of an investment at an amount different from net asset value per share is probable, the practical expedient may not be applied

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## Investment Definition

- A security or other asset that a government holds primarily for the purpose of income or profit and with a present service capacity that is based solely on its ability to generate cash or to be sold to generate cash
  - Service capacity refers to a government’s mission to provide services
  - Held primarily for income or profit—acquired first and foremost for future income and profit

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## Fair Value Application

- Assets that meet the definition of an investment generally should be measured at fair value
  - Alternative investments
  - Equity securities, stock warrants, and stock rights that do not have readily determinable fair values – provided such investment-types are not reported according to the equity method
  - Commingled investment pools that are not government-sponsored
  - Invested securities lending collateral
  - Intangible assets
  - Land and land rights
  - Real estate
  - Lending assets
  - Natural resource assets

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## Investments Not Reported at Fair Value

- Money market investments and participating interest-earning investment contracts that have a remaining maturity at time of purchase of one year or less, reported by governments other than external investment pools
- Investments in 2a7-like pools
- Investments in life insurance - investments in life settlement contracts, however, should be at fair value
- Investments in common stock that meet the criteria for applying the equity method
- Non-participating interest-earning investment contracts
- Unallocated insurance contracts
- Synthetic guaranteed investment contracts that are fully benefit responsive

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## Application of Acquisition Value

- Acquisition value (an entry price) replaces fair value for the following:
  - Donated capital assets
  - Donated works of art, historical treasures, and similar assets
  - Capital assets acquired through a nonexchange transaction
  - Capital assets received through a service concession arrangement

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## Disclosures

- The following information for each class or type of assets and/or liabilities measured at fair value should be disclosed:
  - The fair value measurement at the end of the reporting period and for nonrecurring fair value measurements, the reasons for the measurement
  - The level of the fair value hierarchy within which the fair value measurements are categorized in their entirety (Level 1, 2, or 3)
  - A description of the valuation technique(s)

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## Level 3 and NAV

- For fair value measurements categorized within Level 3 of the fair value hierarchy
  - The effect of those investments on investment income for the reporting period
- Disclosures for investments in certain entities that calculate NAV per share (or its equivalent)
  - Information that helps users of its financial statements to understand the nature and risks of the investments
  - Information on whether the investments are probable of being sold at amounts different from net asset value per share (or its equivalent)

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# GASB Exposure Draft

Accounting and Financial Reporting  
for Certain External Investment Pools

## External Investment Pools

- **What:** The GASB is considering revisions to the accounting and financial reporting standards for 2a7-like investment pools
- **Why:** Securities and Exchange Commission changes to Rule 2a7 would make it difficult for external investment pools to meet the criteria to report as 2a7-like
- **When:** Exposure Draft issued - June 2015

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## Background

- Current standards allow pools that are considered to be 2a7-like to report investments at amortized cost rather than fair value
  - The SEC recently made significant changes to Rule 2a7
  - Concerns were raised regarding the cost-benefit of government pools applying the revised Rule 2a7 provisions
- The project is considering criteria independent of Rule 2a7 that could be applied by external investment pools to determine when a cost-basis can be applied to investments.
  - The current 2a7 provisions and other regulatory provisions are being used as starting point.
- This project would not apply to the NCCMT Cash (Government) Portfolio and the NCCMT Term Portfolio
  - The Term Portfolio is registered with the SEC and is a bond fund
  - The Cash Portfolio is registered with the SEC - not currently affected by the GASB's proposed changes – would have to de-register to benefit from any changes

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## Proposal Summary

- GASB separated accounting and financial reporting from SEC requirements
- ED driven by amortized cost approximating fair value
- Patterned after 2010 SEC regulations for 2a7 funds
- Some of the 2010 regulations were excluded (e.g., stress testing) if they were operational in nature
- Significant instances of noncompliance would require a switch to fair value accounting
  - Professional judgment required
  - Significant means material
  - Switch back to amortized cost possible in future periods

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## Tentative Criteria Categories

- Pool should transact with participants at a stable net asset value (NAV) – if NAV floats an external investment pool should use fair value
- Portfolio maturity limits
- Portfolio quality requirements
- Portfolio diversification requirements
- Portfolio liquidity limits
- Shadow pricing requirements

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## Proposed Implementation

- FY ending after 6/15/15 – except for shadow pricing and credit quality requirements which would be implemented for FY ending after 12/15/15
- External pools choosing to report at fair value after implementation would never be allowed to revert back to amortized cost
- External pools not qualifying for amortized cost in some years might be allowed to use amortized cost in future years under certain circumstances
- External pools using amortized cost would be allowed to switch to fair value in future years

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## Financial Reporting Model Review

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## Financial Reporting Model Review

- GASB 34 finalized in June 1999
- The GASB regularly reviews existing standards to examine effectiveness
- Pre-agenda research to identify how project has been implemented in practice
  - 11 roundtables
  - Surveys of preparers, auditors, and users
  - Review of audited financial reports
  - Literature research
  - 150+ interviews
- Project added to agenda in September – implementation in 2020 – 21 most likely

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