# Government Finance Officers Association

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Ms. Teresa S. Polley Chief Operating Officer



LETTER OF COMMENT NO.

Financial Accounting Foundation

401 Merritt 7 Norwalk, Connecticut 06856-5116

Dear Ms. Polley:

I am writing to you on behalf of the Government Finance Officers Association (GFOA) in response to the Financial Accounting Foundation's (FAF) request for comments on certain Proposed Changes to Oversight, Structure, and Operations of the FAF, FASB, and GASB. The GFOA wishes to focus its comments on four specific proposals that would directly affect the oversight and operations of the Governmental Accounting Standards Board (GASB).

## Nomination and election of government trustees

The FAF currently includes three government trustees. The method used to select those trustees is the product of a carefully negotiated agreement reached in 1984 between the FAF and nine major groups representing state and local governments. That agreement was a precondition for the states agreeing to delegate their inherent power to set accounting standards for governments within their jurisdiction. The nominating process spelled out in that 1984 agreement carefully balances the legitimate interests of the FAF and those of state and local governments. For more than two decades that process has worked smoothly and has resulted in the nomination of trustees of the highest quality who have gone on to serve the FAF with distinction.

Nothing is perfect, of course, so state and local governments naturally are open to any proposed change that would improve the current method of nominating governmental trustees without compromising its essential balance. In that spirit, the GFOA and the National Association of State Auditors, Comptrollers, and Treasurers recently expressed their willingness to consider a change that would allow the FAF to reject nominees deemed unsuitable on the basis of agreed-upon criteria, provided that state and local governments retained the right to select a suitable replacement (see attachment). Unfortunately, the FAF's proposals for changing the method used to nominate governmental trustees reflect an entirely different spirit,

The FAF proposes to jettison *unilaterally* the carefully crafted balance of the 1984 structural agreement, offering in its place no meaningful assurance that the interests of state and local governments would be adequately represented by trustees who enjoyed their confidence. Consequently, the GFOA considers the proposed changes to be a clear breach of both the letter and the spirit of the 1984 structural agreement and *totally unacceptable*. The FAF is responsible for overseeing two standard-setting bodies of equal status—one for the private-sector and one for the public-sector. If the FAF is convinced that it is essential that all trustees be selected in the same manner (the ostensible rationale for the proposed change), it need only agree to alter the composition of the board to include an equal number of governmental and non-governmental trustees. Absent such a change, state and local governments have no choice but to insist that their vital interests be protected by representatives of their own choosing.

## Improved governance and oversight

The GFOA urges the FAF to strengthen and enhance its governance and oversight of the GASB. One of the principal reasons state and local governments originally decided to place the newly formed GASB under FAF oversight was to maximize cooperation between the GASB and its private-sector counterpart, the Financial Accounting Standards Board (FASB). Yet, the GASB seems increasingly drawn in recent years toward setting its own accrual standards for situations *identical* to those found in the private sector and already adequately addressed by private-sector standards (e.g., derivatives, sales and pledges of receivables). With the growing momentum toward global convergence in accounting standards, it now seems more important than ever that any tendency toward unnecessary divergence be kept in check. Accordingly, we believe the FAF should take responsibility for periodically reviewing the technical agendas of both boards to satisfy itself that duplication of effort is minimized and that differences in accounting standards reflect substantive differences in circumstances between the public and private sectors.

### Control of the technical agenda

The technical staff of each board reports to the chair, which gives the chair a significant strategic advantage over other board members. In the case of the GASB, that comparative advantage takes on even greater significance, because the chair is also the GASB's only full-time member. The GFOA believes it would be a mistake to further concentrate power in the chair of the GASB by making the chair the sole and ultimate arbiter of the board's technical agenda. Such a change, in our view, is almost certain to undermine collegiality, converting what had been a group of colleagues with a common mission into a mere sounding board for the chair's positions. Furthermore, we fail to see the "problem" that calls for such a drastic "solution."

#### Board size

The FASB sets standards for a broad range of entities. Of the 16 "industries" for which the American Institute of Certified Public Accountants has issued industry audit guides, 15 fall within the scope of the FASB's jurisdiction (i.e., Agricultural Producers and Agricultural Cooperatives; Airlines; Brokers and Dealers in Securities; Casinos; Common Interest Realty Associations; Construction Contractors; Depository and Lending Institutions: Banks and Savings Institutions, Credit Unions, Finance Companies and Mortgage Companies; Employee Benefit Plans; Entities With Oil and Gas Producing Activities; Federal Government Contractors; Health Care Organizations; Investment Companies; Life and Health Insurance Entities; Not-for-Profit Organizations; Property and Liability Insurance Companies). While it might be argued that the number of GASB board members should be the same as the number of FASB board members, it is difficult to maintain that a board with a narrower scope of authority needs a larger number of board members. Thus, the GFOA believes the time has come to reconsider restoring the GASB to its original composition of just five members, consistent with the revised structure proposed for the FASB.

For over a century the GFOA has been a leading force in promoting improved accounting and financial reporting in the public sector. We remain thoroughly committed to that goal and to the principle of independent standard setting. We are cognizant of the positive role the FAF has played in the past in this regard and commend its willingness to consider new ways to even better meet its objectives. At the same time, we have no choice but to urge the FAF to avoid any precipitous unilateral action that would run the risk of irreparably compromising its credibility and effectiveness with state and local governments.

If you have any questions or wish to discuss any of these matters further, please do not hesitate to contact me.

Sincerely yours,

Jeffrey L. Esser, Executive Director/CEO

Encl.: State and Local Government nominee proposal

cc: Douglas Ellsworth
Edward Harrington
John Radford

Jeffrey R. Ener

The National Association of State Auditors Comptrollers and Treasurers (NASACT) and the Government Finance Officers Association (GFOA) will recommend the following to the nine state and local government organizations that were parties to the 1984 agreement creating the Governmental Accounting Standards Board:

- The National Association of State Auditors Comptrollers and Treasurers
   (NASACT) and the Government Finance Officers Association (GFOA) shall no
  longer be "electors" of the Financial Accounting Foundation (FAF) and nominees
   of the state and local government organizations shall no longer be subject to
   approval by electors.
- 2. The following nine state and local government organizations, hereinafter referred to as "state and local government organizations": National Governors' Association, National Conference of State Legislatures, Council of State Governments, National Association of Counties, National League of Cities, U.S. Conference of Mayors, International City/County mangers Association, National Association of State Auditors Comptrollers and Treasurers and the Government Finance Officers Association will nominate each of the three state and local government trustees to serve on the FAF Board.
- 3. A state and local nominee shall be accepted and elected by the members of the FAF Board of Trustees, unless the FAF Board of Trustees determines that a nominee is not suitable for election as a Trustee.
- 4. The FAF and the state and local government organizations shall agree on a definition of "suitable" designed to eliminate all and only those candidates whose ethics or integrity might reasonably be called into question, including individuals convicted of a crime; individuals under investigation for criminal activity by a local, state, or federal agency; individuals who have been disciplined by a professional or licensing body; and individuals in similar circumstances. A nominee cannot be rejected or in any way discriminated against on the basis of race, color, religion, sex, age, sexual orientation, marital status, national origin, or disability.
- 5. If the FAF Board of Trustees determines that a state and local government nominee is not suitable for election the FAF, the board shall promptly notify the state and local government organizations and ask for the submission of another nominee.