Private Company Financial Reporting Committee
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Judith H. O'Dell CPA CVA
Chair

September 23, 2010

Mr. Robert Herz
Chairman
Financial Accounting Standards Board
401 Merritt 7
Norwalk, CT 06856

Re: Proposed Accounting Standards Update, Amendments for Common *Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs* ("proposed ASU")

Dear Mr. Herz:

The Private Company Financial Reporting Committee has reviewed the proposed Accounting Standards Update titled *Amendments for Common Fair Value Measurements and Disclosure Requirements in U.S. GAAP and IFRSs* and offers the following comments and recommendation. The PCFRC's comments and recommendation are focused on respondent question 7 of the proposed ASU, which addresses the proposed disclosure of a measurement uncertainty analysis.

<u>Respondent Question 7</u>: *The Board has decided to require a reporting entity to disclose a measurement uncertainty analysis that takes into account the effect of correlation between unobservable inputs for recurring fair value measurements categorized within Level 3 of the fair value hierarchy unless another Topic specifies that such a disclosure is not required for a particular asset or liability. Do you think that proposal is appropriate? If not, why not?*

<u>PCFRC Response</u>: On October 12, 2009, the PCFRC issued a letter to the FASB about Proposed Accounting Standards Update, *Improving Disclosures about Fair Value Measurements*. In that letter, the PCFRC provided comments and a recommendation about proposed "sensitivity disclosures", which are similar to the proposed measurement uncertainty analysis disclosures in the current proposed ASU. The PCFRC reiterates those comments and recommendation, which follow.

If private companies prepare and disclose fair value measurements, those fair value measurements are frequently based on unobservable inputs (Level 3). As such, the measurement uncertainty analysis put forward in the proposed ASU would extensively affect the private company sector and are therefore of serious concern to the PCFRC. The financial statement users on the PCFRC do not believe that the measurement uncertainty analysis would provide them with decision-useful information. Moreover, the financial statement preparers and practitioners on the Committee believe that the measurement uncertainty analysis will impose a cost burden on private companies and increase their litigation risk as some users may misunderstand the nature of the disclosures.

User Needs and the Problematical Nature of a Measurement Uncertainty Analysis

Conducting a measurement uncertainty analysis on Level 3 fair value unobservable inputs is problematical in the private company sector. Most Level 3 valuations for private companies do not involve valuation models with inputs for which a reasonable range of alternatives may exist. Level 3 valuations for private companies generally consist of valuations of businesses or business units which involve a high degree of subjectivity and judgment. There are many inputs which have a wide range of reasonably possible alternatives and a great deal of subjectivity would be present as companies struggle with the extent and range of their analyses. Magnifying the problem is the lack of market-based inputs in the private company sector, making it more difficult to determine a reasonable range for purposes of conducting a measurement uncertainty analysis. Clearly, comparability will suffer as different private companies make different judgments about the range of reasonably possible alternative Level 3 inputs.

The financial statement user members of the PCFRC fail to see the benefit derived from a measurement uncertainty analysis. The existing requirement to identify fair value measurements in the financial statements as being based on Level 3 inputs already serves as a red flag to users. The additional analysis does not provide decision useful information to private company users and may be counter productive by creating confusion and additional "noise" in the financial statements. Also, the lack of comparability and the short-lived, snapshot nature inherent in a measurement uncertainty analysis further renders it less relevant to private company users.

Cost Burden and Second-Guessing

The financial statement preparers and practitioners on the PCFRC agree that conducting a measurement uncertainty analysis of Level 3 measurements and preparing the related disclosures would be a costly exercise for private companies. Costs include the sophisticated work involved in developing the range of reasonably possible alternative inputs, the possibility of having to engage outside sources to develop the alternative inputs, the high level of work needed to justify such inputs, and documenting the work. The lack of market inputs in the private company sector may result in a broader range of reasonably possible alternative inputs and therefore increased cost. Further, additional audit work would need to be performed on the analysis and disclosures.

The PCFRC is also concerned that disclosing reasonably possible alternatives in the financial statements exposes preparers and practitioners to increased "second guessing" by financial statement users. The proposed measurement uncertainty analysis may unintentionally imply a level of certainty that does not exist. This could prove detrimental to financial reporting users and cause litigation problems for preparers and practitioners.

Recommendation

The PCFRC notes that the proposed ASU states "the amendments in this proposed Update would result in common fair value measurement and disclosure requirements in U.S. GAAP and IFRS." The PCFRC reminds the FASB that the IASB does not have to consider non financial institution private companies since the issuance of IFRS for SMEs. IFRS for SMEs' Basis for Conclusions paragraph BC 107 notes that "many of the IFRS 7 disclosures are designed for financial institutions (which are ineligible to use IFRS for SMEs) or for entities whose securities are traded in public capital markets" and exempted small- and medium-sized entities from the IFRS 7 disclosures. Required disclosures in the IFRS for SMEs document (paragraph 11.43) for financial instruments measured at fair value consist of the basis for determining fair value (for example, quoted market price or a valuation technique.) When a valuation technique is used, the entity shall disclose the assumptions applied in determining fair value for each class of financial assets or financial liabilities. When considering the needs of users of private company financial statements, the IASB did not believe that disclosing a measurement uncertainty analysis was necessary.

Futhermore, while we acknowledge that the measurement uncertainty analysis will only apply to fair value measurements in Level 3 that are made on a recurring basis, this change from the original proposal at present limits the effect of this proposal. Of course, if the proposed ASU on accounting for financial instruments passes as currently written, the sweep would be much broader

Based on the reasoning presented above, the PCFRC does not believe that the measurement uncertainty analysis put forward in the proposed ASU passes the user needs/cost benefit test in the private company sector. Consequently, the PCFRC recommends that the FASB exempt private companies from the measurement uncertainty analysis disclosures.

The PCFRC appreciates the FASB's consideration of these comments and recommendation. Please feel free to contact me if you have any questions or comments.

Sincerely,

Judith H. O'Dell
Chair
Private Company Financial Reporting Committee