## DUFF&PHELPS



LETTER OF COMMENT NO. 9

November 22, 2006

Director, TA&I—FSP Financial Accounting Standards Board 401 Merritt 7 P.O. Box 5116 Norwalk, CT 06856-5116

**RE: Proposed FSP FAS 141-b, 142-e, and 144-b** 

Duff & Phelps appreciates the opportunity to submit our comments with regard to the subject Proposed FSP FAS 141-b, 142-e, and 144-b. We would be pleased to further discuss our comments and responses with the Board and staff. Please direct any questions to Paul Barnes in our Philadelphia office at 215-430-6025.

Sincerely,

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## **Market Participants**

A critical concern of ours is the lack of guidelines for the identification of Market Participants (and thus the assumptions that would be used by Market Participants) which will continue to contribute to inconsistent interpretations of the appropriate basis for a valuation as well as the inputs into the valuation process. A significant amount of judgment remains in the identification of Market Participants and their related assumptions. Diversity in the outcome of valuations, given the same facts and circumstances, will result based on judgments required as to the identification of the appropriate Market Participants and their hypothetical views.

We believe more guidance is necessary with regard to the definition and application of Market Participants including, but not limited to, the following:

- In the identification of Market participants, is it those companies that are the logical pool of buyers (1) of the entire business or (2) of each component asset that needs to be valued apart from goodwill.
- How should the different operating characteristics of a strategic buyer versus a financial buyer, both of whom may bid a similar amount, be evaluated in defining the characteristics of the Market Participant?
- What is the level of cost and effort that is "undue" and therefore need not be expended in the attempt to identify reasonable assumptions that a Market Participant would employ.

## **Adjustment For Risk**

Among those examples that this proposed FSP does *not* address is: (c) whether an adjustment for risk must be included in a fair value measurement. We assume that this example does not intend to indicate that an appropriate risk premium should not be included in the derivation of the discount rate to be applied to the expected cash flows in a fair value measurement using a discounted cash flow approach.

## Paragraphs 8 and 9

Our understanding of ¶8 is that it deals with the situation in which a specific buyer will remove from the marketplace ("lock up") an acquired asset. If there is information (that is reasonably available without undue cost and effort to that specific buyer) that a market participant would use the subject asset, that information should be reflected by the buyer in the fair value measurement. However, if there is no information (that is reasonably available without undue cost and effort to that specific buyer) that market participants would use different assumptions, then the fair value measurement would be based on the buyer's own assumptions including the defensive value

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expected to be provided by the acquired asset. Because this paragraph is silent on the time between acquisition and lock up, the lock up of the acquired asset could presumably occur either immediately or after a transition period of use by the buyer.

Our understanding of ¶9 is that it deals with the situation in which a specific buyer will use an acquired asset for a transition period until the buyer can substitute one of its own assets with similar or greater utility at which time the acquired asset will be discontinued and abandoned. If there is information (that is reasonably available without undue cost and effort to that specific buyer) that a market participant would use the subject asset for a period greater than the buyer's transition period, that information should be reflected by the buyer in the fair value measurement. However, if there is no information (that is reasonably available without undue cost and effort to that specific buyer) that a market participant would use different assumptions, then the fair value measurement would be based on the buyer's own assumptions reflecting the use of the acquired asset only for the transition period.

We are not certain we fully understand the distinction that is meant to be identified in ¶8 and ¶9. The guidance appears to be identical with the difference being the consideration of defensive value in ¶8 versus transition value in ¶9 in those cases where there is no information that a market participant would use different assumptions. Does the use of defensive value or transition value depend on the nature of the asset? That is, was acquired technology in ¶8 meant to be illustrative of the types of assets for which defensive value would apply? If so, what other types of assets (e.g., those assets to be commercialized in the external marketplace) would fall within the defensive value category? Was acquired internal-use billing software in ¶9 meant to be illustrative of the types of assets for which transition value would apply? If so, what other types of assets (e.g., those assets to be used for internal-use only and not commercialized in the external marketplace) would fall with the transition value category?

We are also concerned about the incongruent treatment of acquired assets between a specific buyer and a market participant for an identical transaction. For example, in the case of an acquired trade name to be discontinued by the buyer due to the buyer's decision to use its own trade name, for which information indicates that a market participant would use the trade name, the buyer would record the asset at a fair value reflective of the value in the hands of a market participant. Assuming this is an indefinite-life intangible asset in the hands of a market participant and the acquired business and this trade name increase in value post-acquisition, the market participant would have no amortization or impairment charges related to the acquired trade name.

On the other hand, the specific buyer will book the trade name at the same value as the market participant but would amortize it over a relatively short time frame, resulting in significant amortization charges for an asset the buyer is not using. The useful life to the buyer would need to reflect the fact that since the trade name is being discontinued and will no longer receive advertising and marketing support, its recognition and value will decline rapidly over a short period of time.

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If no information regarding market participant assumptions is available as to the use of this trade name, it is unclear whether the provisions of ¶8 (defensive value) or ¶9 (transition value) apply. If transition value is operative, this would probably result in a relatively low value and short life reflective of the temporary use of the trade name until such time as the migration to the buyer's trade name is completed. The basis of this valuation would be entity specific transition data and assumptions.

However, if defensive value is operative, this would presumably require a "with and without" analysis of the buyer's business in order to estimate the incremental value to the buyer (most likely evidenced by enhancement or preservation of the buyer's trade name) of locking up the acquired trade name. From an implementation standpoint, it hard to envision conducting this analysis without significant insight into the market dynamics of the buyer and its competitors (i.e., market participants) and their actual and hypothetical use of trade names, which runs counter to the initial supposition that no information about market participants is available.

The defensive value determination is also is a very hypothetical analysis which has the potential to produce a wide diversity of practice and results.

Finally, assuming that a defensive value can be reliably measured, it appears to record an unusual asset. That is, the defensive value will be ascribed to the acquired trade name and such asset will be recorded and amortized. Presumably, it will be amortized over the life of the asset for which it is providing the economic (defensive) benefit, that being the buyer's existing trade name. In most cases, this will result in the acquired trade name remaining on the balance sheet with an annual amortization charge for many years subsequent to the acquired trade name being discontinued and removed from the marketplace.