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LETTER OF COMMENT NO. 145

August 8, 2008

Technical Director – File Reference No. 1600-100  
Financial Accounting Standards Board  
401 Merritt 7  
P.O. Box 5116  
Norwalk, Connecticut 06856-5116

Re: Proposed Statement of Financial Standards, Disclosure of Certain Loss  
Contingencies (an amendment of FASB Statements No. 5 and 141(R))

Dear Technical Director:

In connection with the proposed Statement of Financial Standards, Disclosure of Certain Loss Contingencies (an amendment of FASB Statements No. 5 and 141(R)) (the "Exposure Draft"), Mayer Hoffman McCann P.C. ("MHM"), appreciates the opportunity to express its views regarding the possible impact the Exposure Draft will have on the financial accounting and disclosures for loss contingencies. Our observations relate primarily to the auditor's ability to adequately assess compliance with the requirements of the Exposure Draft, the potential for abuse of the prejudicial exemption and the possible necessity of the use of an expert by the auditor in the identification and evaluation of contingent legal liabilities.

We are concerned that the Exposure Draft's requirement for enhanced disclosure will lead to frequent disputes between management and its auditors regarding the need for auditors to obtain information to corroborate management's assertions underlying its disclosures regarding loss contingencies. As management and its legal counsel attempt to balance compliance with the proposed disclosure requirements with their desire to protect the interest of the company, it is likely that situations will develop that will cause the auditor to issue a qualified opinion or be unable to report at all. We believe that the current treaty between the American Bar Association and the AICPA does not provide auditors' access to the level of information necessary to satisfy the requirements of U.S. generally accepted auditing standards given the expanded disclosure requirements contained in the Exposure Draft.



We are concerned that many companies will contend that all situations involving legal contingencies are prejudicial thereby reducing the effectiveness of the proposed new disclosures. Additionally, the determination of what is actually prejudicial is a matter of law and companies' counsel are advocates for their clients. Therefore, it will be exceedingly difficult if not impossible for auditors to evaluate this determination without the assistance of their own legal expert. This, of course, would set up the potential for even more confrontation between auditors and their clients and increase the cost of the audit.

MHM supports the Financial Accounting Standards Board in its quest to improve financial reporting related to loss contingencies. However, we believe that in order to maximize the effectiveness of the Exposure Draft and avoid undue tension between competing constituencies in the financial reporting process, the various roles in the process need to be further refined and balanced. Given the importance of legal expertise in the assessment and eventual disclosure of loss contingencies, we believe that greater involvement and the acceptance of greater responsibility for the conclusions reached by the company's legal counsel (whether internal and/or external) is a necessity. In our experience, too often the response received from legal counsel related to an auditor inquiry is evasive, lacks substantive disclosure of the facts and fails to add value or offer any opinion relative to the required financial statement impact and disclosures. This has the result of leaving management and the auditors to work out the disclosure solution while the true legal expert sits on the sidelines. In addition, the attorney representing the Company is not objective and is not working on behalf of investors and auditors. Their client is the Company and this role may place them in a position whereby the interests of the Company and the interests of the financial reporting user community are competing. This necessitates the need for the auditor to employ legal expertise to provide the objectivity necessary to render an opinion on the financial statements as it relates to these areas of expertise. This would clearly have an additional incremental cost to the audit process to effectively comply. Clearly the attorney-client privilege and other legal protections must play into the overall equation; however, with the issuance of the Exposure Draft, an opportunity exists to reevaluate the financial reporting model related to loss disclosures and fully integrate the legal experts into the process to meet the objectives of the Exposure Draft.

Accordingly, we recommend the Board explore the concept of the Company using a "named expert," (as utilized by the Securities and Exchange Commission in its filings), in connection with the financial reporting related to loss contingencies. In other words, if a company has identified legal contingencies, it must engage an expert to evaluate them. In its financial reporting, the company would then be required to name the expert and their conclusion as the basis for the determinations about the facts of the case and the ultimate outcome related to each contingency. The expert would also assist management in the application of the prejudicial exemption thereby reducing the potential for abuse in this area. Once the legal expert has completed their work, the Company would then apply



SFAS 5 using those facts (as opined upon by a named expert) and the auditor would attest to whether SFAS 5 was applied correctly (as opposed to whether the company evaluated all of the facts in the case correctly). We believe the approach described above is likely to lead to increased reliability in the disclosures required by the Exposure Draft. This is an important consideration given the concern that many have expressed regarding the potential for additional litigation should such disclosures fail to be accurate and reliable.

We sincerely appreciate the opportunity to present our views. In summary, we have concerns that, without significant changes to the current agreement between the American Bar Association and the AICPA as noted above, the auditing profession will be unable to obtain the information necessary to fulfill its responsibilities under current auditing standards. We believe the enhanced disclosure requirements included in the Exposure Draft require greater involvement of legal counsel. Although we understand that the Board is not positioned to deal with this matter solely on its own, we urge the Board to delay the issuance of the standard until such matters have been adequately addressed by all parties to which such matters pertain.

Sincerely,  
Mayer Hoffman McCann P.C.

*Mayer Hoffman McCann P.C.*