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October 8, 2008

Mr. Russell G. Golden
FASB Technical Director
Financial Accounting Standards Board
401 Merritt 7
Norwalk, CT 06856-5116



LETTER OF COMMENT NO. 25

Re: File Reference – Proposed FSP FAS 157-d

Dear Mr. Golden:

Our firm, *Financial Reporting Advisors, LLC*, provides accounting and SEC reporting advisory services, litigation support services, and dispute resolution services. We specialize in applying generally accepted accounting principles to complex business transactions. We appreciate the opportunity to comment on the referenced document.

We sincerely appreciate the FASB's willingness to illustrate the application of FASB Statement No. 157, *Fair Value Measurements*, (Statement 157) to financial assets that are not actively traded. Particularly when markets are struggling with unanticipated levels of volatility, uncertainty and illiquidity, an example of the application of Statement 157 may help those who are concerned about the reliability of observable data and the degree to which observable inputs may be adjusted for purposes of estimating fair value. We firmly support the use of fair value measures in financial reporting and believe the resulting information is important to all constituencies, not just investors and creditors. Clearly the complexities of certain instruments combined with the lack of liquid, transparent markets create difficulty in developing fair value estimates. Especially in these circumstances, knowledgeable, diligent people exercising reasonable judgment may differ in the amount that they believe represents a good faith estimate of fair value. Accordingly, discussion and examples that help narrow the differences in good faith estimates will be helpful. But we strongly believe that estimates of the fair value of financial assets following the principles in Statement 157, while imperfect, are critical to the long-term viability of our capital markets.

We agree that the example in the proposed FSP is fully consistent with the definition of fair value in Statement 157. The example makes clear that there are situations in which observable transactions or broker quotes are not determinative in estimating fair value, while also reinforcing that the goal of any fair value measure continues to be the price at which the asset would transfer in a current market transaction, and that, as such, observable market phenomena such as discounts for liquidity cannot be ignored in estimating fair value.

However, we are not certain how helpful the example will be in practice. Although the example reaches conclusions that are not unreasonable on the surface, the underlying rationale is not presented. Absent an explanation of how judgment was applied, we suspect the example will be of limited use in other fact patterns. Specifically:

- We do not understand how the observable inputs referred to in paragraph A32B were “appropriately considered” by Entity A in developing its estimates. For example, if prices for the few observable transactions imply an abnormally high rate of return, would it be appropriate to ignore those transactions on the basis that such a return is indicative of forced sales? Alternatively, what if the few observable transactions imply, say, a 30-35 percent return? In that case, how would Entity A conclude that its estimated 20 percent return reflects the market’s current perspective on credit spreads or liquidity risk premiums? Might the difference be attributable to different estimates of future cash flows of the underlying collateral (e.g., different prepayment or default assumptions)? Said more directly, is there an expectation that Entity A can reconcile its estimate to the observable, albeit stale or limited, market data or is it sufficient for Entity A to note that its estimate is directionally consistent with these few observable transactions compared to the last active market transaction?
- If Entity A had not obtained a nonbinding quote, it logically would have concluded that its estimate (i.e., the one that yields a 20 percent return) was fair value. It would not have had two indicators of the appropriate rate of return, as discussed in paragraph A32E. The implication is that two companies with otherwise identical facts may reach different fair value estimates solely because one obtained a nonbinding quote and the other did not. We suggest that the example explain why, in this case, the nonbinding quote has sufficient weight to alter Entity A’s fair value estimate and, by implication, when it might not.
- We would encourage the FASB to address the way in which the underlying cash flow estimates are developed. We suggest that the example state that the cash flows are estimated by Entity A and explain how observable market data has been incorporated into those estimates.

More broadly related to the proposed FSP, we encourage the FASB to consider the following:

- Explicitly state that the FSP does not amend Statement 157. We recognize that adding an example to a previously issued standard meets the dictionary definition of an amendment. However, we believe some constituents view the SEC Staff’s guidance and this proposed FSP as changing the definition of fair value in Statement 157 by “relaxing” or “loosening” the requirement to consider current market data in estimating fair value. While paragraph A32F notes that the new example is in accordance with the requirements of Statement 157, other aspects of the proposed FSP (such as the need for an effective date, references to accounting for changes in valuation techniques) and the use of words such as “amend” and “clarify” may be fueling the confusion.
- Include an example in which there are no observable inputs for a financial asset that previously was traded in a fairly active market, for example, auction rate securities for which observable data no longer exists.
- Delete or revise the last sentence of paragraph 10 of the proposed FSP. We find that sentence confusing. It implies that paragraph 33 (disclosures for assets measured at fair value on a non-recurring basis) of Statement 157 requires more information than paragraph 32 (disclosures for assets measured at fair value on a recurring basis). We were not aware of an inconsistency in those disclosure requirements. Specifically, the requirement in paragraph 33c to describe significant unobservable inputs and the information used to develop those inputs seems consistent with the first sentence of paragraph 32.

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- Include the guidance in the SEC Staff's September 30, 2008 press release in an appendix to the final FSP. Given that paragraph 6 of the proposed FSP explicitly references the SEC Staff guidance, placing that guidance in the body of the FSP improves its accessibility

In summary, we believe that the example in the proposed FSP will provide limited assistance to preparers, auditors and other constituents. It likely will be helpful to those who may have inappropriately read Statement 157 to say that observable inputs or broker quotes are always determinative of fair value. However, we do not believe it will assist those who are trying to determine the extent to which observable inputs or broker quotes should be adjusted or incorporated in determining the fair value of financial assets in illiquid markets.

We would be pleased to discuss our comments with you at your convenience.

Very truly yours,

Financial Reporting Advisors, LLC

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