Texas Society of
CPA Certified Public Accountants

LETTER OF COMMENT NO. 12

March 2, 2007

Technical Director
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

RE: File Reference 1510-100

To Whom It May Concern:

One of the expressed goals of the Texas Society of Certified Public Accountants (TSCPA) is to speak on behalf of its members when such action is in the best interest of its members and serves the cause of Certified Public Accountants in Texas, as well as the public interest. The TSCPA has established a Professional Standards Committee (PSC) to represent those interests on accounting and auditing matters. The committee has been authorized by the Texas Society of CPAs' Board of Directors to submit comments on matters of interest to the committee membership. The views expressed in this letter have not been approved by the Texas Society of CPAs' Board of Directors or Executive Board and, therefore, should not be construed as representing the views or policy of the Texas Society of CPAs.

We appreciate the opportunity to provide input into your deliberations on the above-referenced Exposure Draft (ED) dealing with derivative instruments and hedging activities.

The members of the PSC were in general agreement with the direction and guidance included in the proposed Statement. We have provided comments on the various issues discussed in the ED and have organized these comments by issue number.

Issue 1—Do you agree with the Board's decision to exclude from the scope of this proposed Statement prescriptive guidance about how derivative instruments should be presented and classified in the financial statements? Why or why not?

We are in agreement with the decision to exclude prescriptive guidance about how derivative instruments should be presented and classified in the financial statements as long as guidance on these issues is forthcoming. We do not believe delaying the disclosures required in this ED to resolve presentation and disclosure issues is warranted because the disclosures required by this ED are not affected by financial statement presentation and classification (although upon resolution of presentation and classification issues, reconsideration of these disclosures may be warranted). We urge the Board to provide guidance on presentation and classification issues as soon as possible. We do not believe open issues should be left unaddressed due to the costs of uncertainty in accounting requirements, which include, but are not limited to, the legal risks that practitioners are exposed to and the diversity of practice that will undermine comparability.

Issue 2—Do you agree that this proposed Statement should apply to both public and private entities? Why or why not?

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We are not in favor of a distinction between public and private GAAP and agree that the proposed Standard should apply to both public and private entities. However, we do encourage the Board to consider the cost/benefit of the requirements of this ED and FAS 133 overall, for entities with limited derivative positions and/or activity. We do not believe this is a public versus private company issue; rather, it is a matter of the significance of derivative positions, activity to an entity's financial position, the results, and the users' understanding thereof. We believe users and preparers would be well served by additional guidance as to when the costs and complexity inherent to derivative accounting and disclosure is warranted and when it is not. One approach would be to allow entities to opt out of certain accounting and/or disclosure requirements with notice of the election and the reasons in the notes to the financial statements.

Issue 3—Do you foresee any significant operational concerns or constraints in compiling the information in the format required by this proposed Statement? Are there any alternative formats of presentation that would provide the data more concisely?

We don't see an issue with compiling the information regarding the breakout of derivatives. We believe that those entities having implemented FAS 133 should already have their derivative documentation cataloged and classified, including notional amounts and fair values. We find the tabular format to be very informative, and believe it will improve the consistency and understanding of derivative disclosures.

Issue 4—This proposed Statement would require disclosure of (a) the existence and nature of contingent features in derivative instruments (for example, payment acceleration clauses), (b) the aggregate fair value amount of derivative instruments that contain features, and (c) the aggregate fair value amount of assets that would be required to be posted as collateral or transferred in accordance with the provisions associated with the triggering of the contingent features. Do you foresee any significant operational concerns or constraints in compiling that information for this disclosure?

We do not see the compilation of such disclosure information posing any significant operational concerns. Members of our committee who have gone through credit reviews on interest-rate derivative products report that counterparties generally understand the terms of credit, the level of open line available, and what the requirements are for collateral or margin posting.

Issue 5—Do you agree that this proposed Statement should require the disclosure of notional amounts? Why or why not?

We believe the disclosure of notional amounts is an appropriate requirement.

Issue 6—Do you agree that the proposed Statement should not require the disclosure of the aggregate notional amounts related to derivatives that no longer exist at the end of the reporting period? Why or why not?

We agree with excluding this information. Disclosure of activity during the reporting period has value, but we do not see any value to disclosure of aggregate notional amounts related to derivatives that no longer exist at the end of the reporting period.

Issue 7—Do you agree that information about "hedged items" that are not in designated and qualifying Statement 133 hedging relationships should be excluded from the disclosure tables? Alternatively, should the tables include gains and losses on "hedged items" that are recorded at fair value and are used in hedging relationships not designated and qualifying under Statement 133? Why or why not? Would your answer be affected by the forthcoming FASB Statement on the fair value option for financial assets and financial liabilities, which will provide the option to report certain financial assets and liabilities at fair value?

We agree that this information should be excluded from the disclosure tables, unless the FAS 159 fair value option is used for hedged items that are not designated and qualifying under FAS 133 ("other hedged items" or "OHI"). We believe mixed disclosure of GAAP designated and qualifying hedges ("GHI") and OHI effectively could create a question as to the accuracy of the reported financial position and results. However, availability of the fair value option under FAS 159 should allow entities in those circumstances to achieve net hedged result reporting and reveal ineffectiveness. Accordingly, we believe inclusion of gains and losses on OHI that are recorded at fair value should be allowed, but with clear distinction and identification of GHI and OHI. If, however, the entity does not elect the fair value option for those items, they should not be included in the tables, but their existence and the inconsistent basis of accounting (between OHI and GHI) should be disclosed.

Issue 8—Do you agree that information that could be provided in the qualitative and quantitative disclosures encouraged by paragraphs 44 and 45 of Statement 133 would be sufficient to appropriately inform users of financial statements about the risk management strategies of an entity? If not, should additional information about an entity's overall risk management strategies be provided as part of the tabular disclosure required by this proposed Statement?

We believe that the nonderivative instruments that a company may use in managing risk should be disclosed separately and not included in the disclosures with those meeting the definition of derivatives. A number of these instruments may be better explained in narrative form as opposed to the tabular requirements for derivative instruments. We support leaving the decision to the judgment of the issuers as to whether their activities are better presented quantitatively or in a narrative format.

Issue 9—This proposed Statement includes examples of qualitative disclosures about objectives and strategies for using derivative instruments, contingent features in derivative instruments, and counterparty credit risk. Those examples are intended to illustrate one potential way of communicating information about how and why an entity uses derivatives and the overall effect of derivatives on an entity's financial position, results of operations, and cash flows. The examples are not intended to be construed as the only way to comply with the disclosure requirements.

Are those examples helpful in communicating the objectives of providing information on how and why an entity uses derivatives and on the overall effect of derivatives on an entity's financial position, results of operation, and cash flows? Or, do you believe those examples would be viewed as a prescribed method to comply with the requirements of this proposed Statement?

We acknowledge the risk of examples being applied as the standard, but we believe this risk is outweighed by the need for clarification that only examples can provide and can be mitigated (but not eliminated) by clear, repetitive reminders about the purpose and limitations of examples. We believe the concepts embodied in this proposed Standard need to be expanded upon by the liberal use of examples. The concepts are complicated and vague, and practitioners need examples to understand the objectives of the proposed Standard. We believe the Board should expand qualifying language in the introduction of each example to make sure it is clear that this is an example and each entity's disclosure should be somewhat unique to reflect that entity's circumstances. We believe presentation of the examples as a separate Appendix helps to convey the purpose and limitations of the examples. The number of examples should be expanded to demonstrate a broader range of the use and effect of derivative instruments.

Issue 10—The Board considered but decided against requiring additional disclosures as described in paragraphs B55—B63. Those disclosures focused on providing information on an entity's overall risk management profile, methods for assessing hedge effectiveness, and situations in which an entity could have elected the normal purchases and sales exception.

Do you agree with the Board's decision not to require disclosures in those areas? Why or why not?

We agree with the Board's decision not to require the additional disclosures described in paragraphs B55—B63. The importance of this information and the need for disclosure should be a matter of judgment.

Issue 11—The Board's goal is to issue a final Statement by June 30, 2007. The proposed effective date would be for fiscal years and interim periods ending after December 15, 2007. At initial adoption, comparative disclosures for earlier periods presented would be encouraged, but not required. Beginning in the year after initial adoption, comparative disclosures for earlier periods presented would be required.

Does the effective date provide sufficient time for implementation?

It's difficult to give a definitive statement regarding the amount of time that would be sufficient for all affected organizations. Six months may not be a sufficient amount of lead time for many companies and public accounting firms to implement the guidance in this proposed Standard, especially considering the application of numerous new auditing standards in this same time period. Thus, we believe the Board should consider a one-year period from issuance to required implementation. However, the Board should encourage early application by those entities with the ability to do so.

We appreciate the opportunity to provide input into the standard setting process.

Sincerely,

Sandra K. Johnigan, CPA, CFE
Chair, Professional Standards Committee
Texas Society of Certified Public Accountants