

LETTER OF COMMENT NO. 325

2101 L Street NW
Suite 400
Washington, DC 20037
202-828-7100
Fax 202-293-1219

www.aiadc.org

April 1, 2009

Financial Accounting Standards Board Attn: Technical Director 401 Merritt 7 Norwalk, CT 06856-5116

Transmitted Via E-mail: director@fasb.org

Re: Proposed FASB Staff Position No. 157-e,

Determining Whether a Market for a Financial Asset is Not Active and a Transaction is Not

Distressed

File Reference: Proposed FSP FAS 157-e

The American Insurance Association ("AIA") is pleased to provide the following comments with respect to the proposed FSP referenced above. The AIA is a leading property-casualty insurance trade organization, representing 350 insurers that write more than \$123 billion in premiums each year. The member companies of AIA are major participants in the capital markets, holding billions of dollars in investments. As such, insurers are directly impacted by the guidance that is proposed by this FSP.

We appreciate the efforts of the Financial Accounting Standards Board ("FASB" or "Board") to provide additional guidance for applying fair value measurements in the difficult market environment that currently exists. Determining a value that is relevant in such markets requires analyses of all relevant factors, not just the mechanical application of one input that may or may not be relevant under current market conditions. We believe the proposed guidance is a step in the right direction and we hope it will provide financial statement preparers with the necessary framework with which to move forward with the analytical judgment that is always needed in preparing estimates, especially under the existing market conditions.

We have a few suggestions that we believe will clarify the intent of this proposed FSP.

<u>Paragraph 11 of the proposed FSP</u>. We note that the proposed FSP clearly states that
the list of factors should not be considered all inclusive. We also note that the next
paragraph focuses on the use of judgment when considering all significant and relevant
factors. For greater clarity, we suggest modest changes in the wording of paragraph 11

of the FSP, and corresponding changes in new paragraph 29A of FAS 157, to appear as follows:

- 11. Step 1 provides factors that indicate that a market is not active. Those factors should not be considered all inclusive because other factors may also indicate that a market is not active. Factors **may** include:
- a. Few recent transactions (based on volume and level of activity in the market, as compared to previously normal market conditions). Thus, there is not sufficient frequency and volume to provide pricing information on an ongoing basis.
- b. Price quotations are not based on current information.
- c. Price quotations vary substantially either over time or among market makers (for example, some brokered markets).
- d. Indexes that previously were highly correlated with the fair values of the asset are demonstrably uncorrelated with recent fair values.
- e. Abnormal (or significant increases in) liquidity risk premiums or implied yields for quoted prices when compared with reasonable estimates (using realistic assumptions) of credit and other nonperformance risk for the asset class.
- f. Abnormally wide bid-ask spread or significant increases in the bid-ask spread. g. Little information is released publicly (for example, a principal-to-principal market).
- Paragraph 13 of the proposed FSP. The second sentence of this paragraph is somewhat problematic. Our reading of this paragraph leads us to believe that a conclusion in Step 1 that the market is not active must lead to a presumption for preparers that a quoted price is associated with a distressed transaction. We believe this presumption is a reasonable approach when markets are inactive. However, the remaining language, beginning with "unless the reporting entity", creates an inherent tension between Steps 1 and 2 that may effectively make the presumption useless.

As currently worded, the proposed FSP would effectively require preparers to affirmatively demonstrate that there is <u>no</u> evidence that there was sufficient time before the measurement date to allow for usual and customary marketing activities for the asset, and that there is <u>no</u> evidence that there were multiple bidders for the asset, in order to retain the presumption that quoted prices are distressed. It is much more difficult – and virtually impossible – to demonstrate that something does not exist than showing that it does exist. Thus, as currently worded, the presumption becomes virtually inoperable.

Since FAS 157 is premised upon active, orderly markets, we believe Step 1 is the only relevant analysis. Accordingly, we recommend that paragraph 13 of the proposed FSP be eliminated and that the current paragraph 14 be re-numbered as paragraph 13 and its language replaced with the following recommended language:

The quoted price, though presumed associated with a distressed transaction, may be a relevant observable input that may be considered in estimating fair value. The reporting entity should consider whether any other factors or conditions warrant making an adjustment to the quoted price as discussed in paragraphs 29 and 29A of Statement 157.

The language of new paragraph 29A would need to be adjusted accordingly.

We believe our recommended changes will restore the use of judgment to its proper role in the analysis of estimated value and provide a practical approach to making the fair value guidance more operational.

- Paragraph 15 of the proposed FSP. In an environment where markets are inactive and quoted prices may be associated with distressed transactions, the use of judgment takes on added importance. Thus, requiring the reporting entity to use a valuation technique other than the presumed distressed quote seems inconsistent with the use of judgment. We suggest that reporting entities be provided with the flexibility of using price quotes when, in the entity's judgment, the quoted prices provide useful information in determining the appropriate value. Instead of stating "the reporting entity must use a valuation...," we recommend substituting 'may' for the word 'must'.
- Examples. We appreciate the short time frame in which this proposed FSP has been drafted. We suggest, however, that the examples provided in this FSP should be reviewed for clarity and consistency with the new guidance. For example, paragraph A32F utilizes market inputs, which appears inconsistent with paragraph 15, which as currently written would prohibit the use of unadjusted price quotes.
- Effective date and transition. We appreciate that the Board wants to provide the ability to apply this new guidance to the first quarter of 2009. Some companies may find that it is operationally more efficient to first apply the guidance in the second quarter. Given that we are nearing the close of the first quarter, we believe that the best approach is to allow preparers the flexibility to assess the implications of adopting this new guidance to their own reporting processes, and to decide for themselves whether to adopt in the first quarter or adopt in the second quarter.

In summary, we support the Board's efforts to provide more clarity in the application of fair value guidance in inactive markets and to make that guidance more operational. We recommend that the Board improve the proposed FSP by making it clear that the listed factors for determining a market is inactive are not all inclusive and that the factor in paragraph 11(a) must be evaluated in light of previous normal markets. We agree with the emphasis on judgment and suggest that the language and examples of the FSP reflect that perspective.

We also believe that proposed Steps 1 and 2 create an inherent conflict that renders useless the presumption that an inactive market yields price quotes that are associated with distressed transactions. Instead, the significance and relevance of those quotes should be considered, along with all other factors, by preparers as they apply judgment in estimating fair value. We recommend that the Board eliminate Step 2 and make adjustments to keep the focus on determining whether the market is inactive and on the significant and relevant inputs that should be considered in estimating fair value.

Finally, we recommend that the Board provide preparers with the flexibility to adopt this FSP either for the interim period ending after March 15, 2009 or the interim period ending after June 15, 2009. Individual preparers are in the best position to determine the operational impact of adopting this guidance and should be provided the necessary flexibility in making that decision. As always, appropriate disclosure of the adoption should be required.

Thank you for this opportunity to comment on the proposed rule. We hope the Board finds these comments helpful. Please feel free to call on us with any questions.

Sincerely,

Phillip L. Carson

Assistant General Counsel American Insurance Association

202.828.7170 (DD); 202.495.7868 (fax)

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pcarson@aiadc.org