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VIA OVERNIGHT MAIL

Technical Director
Financial Accounting Standards Board
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LETTER OF COMMENT NO. 231

Re: Disclosure of Certain Loss Contingencies — Proposed
Amendment of FASB Statements No. 5 and 141(R)
File Reference No. 1600-100

Dear Sir/Madam:

This letter is submitted on behalf of Stanford University, Yale University, Cornell University, University of Pennsylvania, Columbia University, Washington University in St. Louis, Emory University, University of Chicago, University of Rochester, Northwestern University, Northwestern University, and New York University (the “Universities”), to provide comments on the Financial Accounting Standards Board (FASB) exposure draft titled “Disclosure of Certain Loss Contingencies: An Amendment of FASB Statements 5 and 141(R)” (“Exposure Draft”).

Each of the Universities is a private, not-for-profit organization. Each of the Universities nonetheless prepares an annual report including audited financial statements prepared in accordance with GAAP. The annual reports are often publicly available, such as on a university’s website and may be relied upon in financing and banking transactions, including by bondholders who buy a university’s debt. Accordingly, the amendments proposed in the Exposure Draft would directly affect the Universities, which, like many other not-for-profit entities, are often involved in litigation.

Summary

The Universities have significant concerns about the proposed amendments as applied to litigation-related contingencies. The Universities are particularly concerned about the provisions that would require (1) quantitative disclosure of estimates of possible losses, and (2) qualitative disclosure about pending claims. The Universities share the belief, expressed by other commentators, that the significant issues raised by the proposed amendments far outweigh any perceived benefit the additional disclosures might provide.

Specifically, the Universities believe that the additional disclosures proposed by the Board would severely prejudice the Universities' position in litigation. At the same time, the additional disclosures are unlikely to improve significantly the quality of information provided to users of financial statements. For these reasons, the Universities urge the Board not to adopt the proposed amendments to FASB Statements 5 and 141(R).

Alternatively, if the Board is nonetheless inclined to adopt the proposed amendments, the Universities request that the Board exempt not-for-profit entities like the Universities from the scope of the amendments. Whatever perceived benefits may accrue to the users of financial statements issued by public for-profit companies, we are not aware of any suggestion that such additional disclosures are necessary or even desirable for users of the not-for-profit financial statements.

I. **The Universities' Concerns with the Proposed Amendments**

The proposed amendments call for disclosure of all loss contingencies unless the reporting person (referred to here as the "company") has determined that the likelihood of a loss is remote. Even where the likelihood of a loss is deemed remote, the company would still be required to disclose the contingency if it is "expected to be resolved in the near term" and could have a "severe impact" on the company's financial position, cash flows, or results of operations. Since there are relatively few cases, especially in the early stages of litigation, in which the likelihood of loss can be characterized as "remote," disclosure of litigation contingencies could become the rule rather than the exception, with the end product being an estimation of possible loss that would of necessity be speculative and not helpful to users of financial statements.

Under the proposed amendments, companies would be required to make two types of disclosures — "quantitative disclosures" of the amount of damages and "qualitative" disclosures regarding the claims. Both forms of proposed disclosures are extremely problematic.

A. **The proposed "quantitative disclosures" generally could not be made with any degree of precision and would be of minimal value to the public.**

Under the proposal, companies would have to disclose the "amount of [plaintiff's] claim or assessment," or, "if there is no claim or assessment amount, the entities' best estimate of the maximum exposure to loss." If a company believes that those amounts are not representative of its actual exposure, the company would also be permitted to disclose its "best estimate of the possible loss or range of loss." These requirements would be a significant departure from the existing standard, which sensibly requires quantitative disclosure only when a reasonable estimate can be made.

The Universities believe that the requirement to quantify potential exposure in all cases — regardless of whether there is a reasonable basis to do so — is an unrealistic exercise that will be highly prejudicial to them in their defense of litigations to which they are regularly exposed, without providing any significant benefit to the users of their financial statements.

Where a complaint contains a specific damage number, disclosing that amount is straightforward. But that disclosure is unlikely to be useful. Plaintiffs' initial damage demands are often highly inflated and do not necessarily reflect the company's true exposure. While a company could also disclose its "best estimate of the possible loss or range of loss," it is often difficult if not impossible to formulate such a "best estimate." In the early stages of a litigation — before factual investigation of the basis for a claim has been completed — or where information necessary for the calculation of potential damages is largely (or exclusively) in plaintiff's possession, a company will rarely, if ever, be able to make any reliable estimate of potential damages. It can often take months, if not years, before a company has collected the data necessary to calculate even a reasonable potential range of loss.

In many cases a complaint does not specify any amount of damages. In some jurisdictions, plaintiffs are prohibited from stating a damage amount in their complaint. In those cases, under the proposal, the company must calculate and disclose its "best estimate of the maximum exposure to loss." If the company believes the maximum exposure is not representative of its actual exposure, it may also disclose its "best estimate of the possible loss or range of loss." Again, these can be impossible undertakings especially in the early (or even not-so-early) stages of litigation, as the company may not have available to it sufficient information to make a reasonable estimate of either its "maximum exposure to loss" or even the "possible loss or range of loss."

Consider the following examples:

- Plaintiff brings a personal injury claim against a University alleging injury by virtue of defendant's conduct. Plaintiff seeks an unstated amount of compensatory damages for medical costs, loss of work, additional unspecified expenses, and pain and suffering. Plaintiff also seeks punitive damages in an amount to be determined at trial. What is the "maximum amount" of potential liability, or even the "best estimate of the possible loss or range of loss" that should be disclosed? Information necessary to calculate the amount of compensatory damages (medical costs, lost wages, etc.) is entirely within plaintiff's knowledge. And the amount of punitive damages can be arbitrary and certainly unpredictable, depending on the subjective determination of the jury at the end of trial. It is not realistic to expect defendants to calculate a "maximum exposure" or even a "range of loss" with any degree of accuracy. Any number they come up with will be highly speculative and unlikely to provide useful, reliable information to consumers of financial statements.
- A class action is brought against a University alleging discrimination in hiring and promotions, covering thousands of employees over an extended period of time. Calculation of potential damages requires statistical analysis of wages, individual promotion decisions, and wage discrepancies, all of which can take months if not years, to calculate. What would the University be expected to disclose pending that analysis?

- Consider the same discrimination claim above, but plaintiffs seek injunctive or other forms of non-monetary relief that require the University to change its policies. The Exposure Draft fails to suggest how to evaluate lawsuits seeking injunctive or other forms of non-monetary relief.
- A student expelled from the University brings a claim alleging wrongful expulsion and seeking an unstated amount of damages to compensate them for the loss of higher lifetime income had they graduated from an Ivy League University. What number, or range of numbers, would the University disclose as potential damages? Would it depend if the student were a business major or a music major? An 'A' student or a 'C' student?
- Plaintiff brings a contract claim, in which it does not disclose the loss to it of the breach or the claimed damages, none of which is known to the University. How is the University to calculate the "maximum damages" or even a potential range of loss?

Beyond the problem of trying initially to calculate potential damage amounts, damage estimates will frequently change over the course of litigation. Many litigation developments will affect the damage analysis, including: venue; judicial assignment; the court's ruling on a motion to dismiss; whether a class is certified and the scope of any such certification; the scope of discovery ordered by the court, including on issues such as relevance and privilege; counsel's review of the University's internal documents (which may include millions of emails); review of documents received from plaintiff (or even co-defendants or non-party witnesses); witnesses' performance at deposition; whether the trial will be heard by a judge or jury; legal developments and precedents; judicial rulings on experts and damage theories; summary judgment decisions which can end a case or narrow its scope; jury selection; and the course of the trial itself.

Each one of these factors can potentially cause a significant re-evaluation of the potential damages, or even range of damages, that may be incurred in litigation. Over the course of litigation it is possible to have many assessments and re-assessments of likely damages. Financial statements containing ever changing damage estimates are unlikely to prove useful to users of financial statements — while at the same time providing extremely useful information to the plaintiffs in the litigation, who will receive real-time information on the defendants' evolving view of the litigation.

For these reasons, the Universities do not believe it is realistic to require the disclosure of the "maximum exposure to loss," or the "possible loss or range of loss" for a claim, where there is no reasonable basis for their disclosure. Any "guesstimate" calculated by the Universities is unlikely to achieve the Board's goal of providing improved information to the users of financial statements.

B. The proposed "qualitative disclosures" would be of minimal value to the public.

The Exposure Draft would also require the disclosure of qualitative information about a company's litigation contingencies, including a "description of the factors that are likely

to affect the ultimate outcome of the contingency along with their potential effect on the outcome,” “a qualitative assessment of the most likely outcome,” and the “significant assumptions” underlying these assessments. These qualitative disclosures, like the quantitative disclosures, would be extremely difficult to make and are unlikely to provide useful information to users of financial statements.

As with the quantitative disclosures, a University cannot be expected to provide a realistic assessment of the “most likely outcome” of litigation before there has been an opportunity to interview witnesses and review and analyze documents (which can include millions of emails). Nor can there be any realistic assessment of the most likely outcome before there have been judicial rulings on potentially dispositive legal issues, for example where a case may be narrowed or dismissed in response to a motion to dismiss the complaint. In these situations, any estimate or prediction is likely to be pure guesswork without any meaningful analytic basis. Moreover, these assessments will likely evolve continuously throughout the course of litigation, for the reasons identified above. These shifting views on the litigation are unlikely to significantly improve the quality of disclosure for litigation contingencies.

Given the factors noted above, any such disclosure would constitute nothing more than the individual judgment of the University and its counsel. But counsel can have differing views of the significance of a particular forum or judge; of the status of the facts or the law; and on the course of the case generally. Plaintiffs and defendants often have differing views, and indeed co-defendants (and their counsel) often have widely varying views on potential litigation strategy or outcomes. For these reasons, any qualitative disclosures are unlikely to provide useful information to the public. Indeed, one can envision a scenario in which co-defendants in litigation disclose different assessments about the very same litigation — each assessment reasonably held by a different defendant.

C. Both the quantitative and the qualitative disclosures would significantly prejudice the Universities in litigation.

While the quantitative and qualitative disclosures are unlikely to provide materially enhanced information to the public, the disclosures would be extremely prejudicial to the Universities. By requiring a University to disclose its estimate of potential damages, the “factors that are likely to affect the ultimate outcome of the [litigation] contingency along with their potential effect on the outcome” and the University’s “qualitative assessment of the most likely outcome,” the proposed rule would fundamentally alter the adversary system by forcing a defendant to give its litigation adversaries its counsel’s assessment of the strengths and weaknesses of its litigation position. Making such disclosures — and giving plaintiffs real-time insight into a University’s litigation assessment — will almost certainly prejudice a University’s defense of litigation.

First, the qualitative disclosures would make it more difficult for defendant Universities to argue, either before the court or in settlement discussions, that certain theories are inapplicable or certain facts irrelevant if the defendant Universities used such theories or facts to calculate their exposure risk and disclose them to investors. If anything, the disclosures could be

argued to be admissible evidence against the University in the very litigations that are the subject of the disclosure, increasing the likelihood of adverse judgments or higher settlement amounts.

Second, the disclosures will likely affect settlement negotiations between the parties. Early disclosure of a large potential exposure (where it is possible to estimate) is likely to increase the demand from the plaintiff in settlement negotiations and the ultimate cost of resolution, particularly where the disclosed amount exceeds the initial expectations of plaintiff. At the same time, the in terrorem effect of required early "disclosure" of potentially large exposure could well unfairly add to a plaintiff's settlement leverage with little or no regard to the underlying merits of the claims.

Third, these disclosures would effectively force Universities to do plaintiffs' work for them — to come up with all possible theories plaintiffs can argue and the most advantageous damage calculations plaintiffs can devise — and then provide that information to the plaintiffs. The required disclosures may therefore have the effect of pointing plaintiff's counsel to facts or to theories of liability or damages that such counsel might not have developed on its own, again to the significant prejudice of the Universities in the litigation.

Fourth, the proposed draft disclosures could result in judicial findings of waiver of attorney-client privilege and attorney work product immunity that would otherwise protect such assessments from discovery or from use against the University in litigation. Indeed, given the liberal discovery rules in U.S. litigation, the proposed new disclosure standards threaten to subject Universities and their counsel to broad-ranging discovery by plaintiffs regarding the Universities' assessment of litigation and the bases therefor. This is particularly the case in the event, not unlikely, that developing the newly-required disclosure obliges the University to consult with experts or other outside sources of information or data.

Finally, it would be difficult for Universities to work with their auditors to obtain the auditors' comfort with their disclosures and that process could require Universities to disclose materials that they would otherwise retain under attorney-client privilege and possibly further jeopardize their position in the legal proceedings.

For these reasons, the Universities do not believe that the proposed amendments should be adopted.

II. *Not-For-Profit Organizations Should be Exempted from the Amendments, if Adopted*

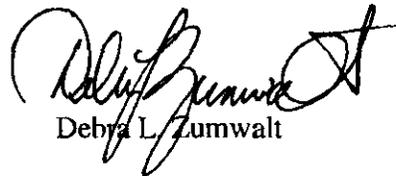
If the Board is nonetheless inclined to amend FASB 5 as proposed in the Exposure Draft, the Universities respectfully request that the amendment exempt not-for-profit organizations from its scope.

According to the Exposure Draft, the Board has proposed the amendments because "[i]nvestors and other users of financial information" have expressed concerns that disclosures about loss contingencies under the current guidelines "do not provide adequate information to assist users of financial statements in assessing the likelihood, timing, and amount of future cash flows associated with loss contingencies." But not-for-profit organizations do not

have shareholders and are not traded on the stock exchanges. The Universities are not aware of any concerns raised by users of their financial statements as to any inadequacies in the current reporting of litigation (or other) loss contingencies. Given that there would be marginal, if any, benefit to the users of not-for-profit financial statements from the additional proposed disclosures, the Universities do not believe such purported benefits could possibly justify the significant costs.

The Board in the past has exempted not-for-profit organizations from certain financial reporting standards. For example, not-for-profit organizations do not need to comply with the pronouncement specific to publicly held companies, such FAS 131 (Disclosures about Segments of an Enterprise and Related Information). Not-for-profits are also excluded from FAS 141 (Business Combinations) and FAS 142 (Goodwill and Other Intangible Assets). Because they are not publicly traded entities, the requirements of Sarbanes-Oxley do not apply to nonprofits. The Universities believe that a similar exemption would be appropriate here. Any hypothetical benefits to the users of financial statements issued by not-for-profit entities cannot conceivably outweigh the significant detriments and costs that would be incurred by compliance with the proposed amendments.

Sincerely,



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