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Mr. Russell G. Golden Technical Director Financial Accounting Standards Board 401 Merritt 7 P.O. Box 5116 Norwalk, CT 06856-5116 08 July 2009

Proposed FASB Staff Position No. FAS 157-g, "Estimating the Fair Value of Investments in Investment Companies That Have Calculated Net Asset Value per Share in Accordance with the AICPA Audit and Accounting Guide, *Investment Companies*"

Dear Mr. Golden:

We are pleased to comment on the proposed Financial Accounting Standards Board (FASB or the Board) Staff Position No. FAS 157-g, "Estimating the Fair Value of Investments in Investment Companies That Have Calculated Net Asset Value per Share in Accordance with the AICPA Audit and Accounting Guide, *Investment Companies*" (the proposed FSP). We commend the Board for providing guidance addressing the challenging issues surrounding the estimation of fair value of investments in investment companies that have calculated net asset value per share in accordance with the AICPA Audit and Accounting Guide, *Investment Companies* (the Guide), herein referred to as alternative investments.

The clarification by FASB Statement No. 157, *Fair Value Measurements* (Statement 157), that fair value represents a current exit price (i.e., the price that would be received to sell the asset in a transaction at the measurement date between market participants that are independent of the reporting entity) has raised questions about the long standing industry practice of measuring certain alternative investments at their net asset value (NAV) per share. While NAV is determined based on the fair value of the investee's underlying investments, the item being measured (i.e., the unit of account) is the reporting entity's interest in the investee, not a pro-rata share of the underlying investments of the investee. As such, the NAV per share may not represent the fair value of the investment in all circumstances because certain features of the investment that could affect its exit price may not be captured in the NAV. For example, NAV would not capture the effect (either positive or negative) on estimated fair value of any unfunded commitments associated with the investment. In addition, while investees stand ready to redeem certain types of alternative investments for NAV per share, many other alternative investments contain restrictions on redemptions or are redeemed only through distributions from the investee. The absence of liquidity provided by investees for these types of investments has raised questions about the use of NAV to estimate a current exit price as of the measurement date.

In contrast to the conceptual issues noted above, many preparers raised practical concerns regarding their ability to determine and support any adjustments to NAV in estimating a 'true exit price' for many types of alternative instruments given the lack of available market data for most of the affected investments. Additionally, investors raised concerns about the reduction in comparability that would result from highly subjective adjustments being made to NAV in estimating the fair value of alternative investments.

The Board's decision to allow for a practical expedient to measure alternative investments within the scope of the proposed FSP using NAV per share, supplemented with additional disclosures, addresses the varying concerns raised by different

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constituent groups. As such, Ernst & Young supports the issuance of the proposed FSP. Our responses to specific questions posed by the Board in the proposed FSP and certain other recommendations are discussed below.

Scope

The proposed FSP would only apply to alternative investments that do not have readily determinable fair values (as defined in FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*). We agree with the Board's approach to scope, as we do not believe it would be appropriate to provide a practical expedient in situations in which the fair value of an alternative investment is readily determinable. To do so, in our view, would call into question the measurement objective for these instruments and further confuse the principles underlying fair value measurements in US GAAP. In addition, such an approach would seem inconsistent with the Board's justification of a practical expedient due to cost/benefit considerations. Presumably the cost and effort involved in the measurement of an alternative investment with a fair value that is readily determinable would not be excessive.

However, we do recommend that the Board clarify that the scope of the proposed FSP would include investments in entities that do not currently report under US GAAP, (e.g., certain foreign funds), but which carry all their underlying investments at fair value and would be subject to the Guide if they were subject to US GAAP. While we believe this was the Board's intent, the wording in the proposed FSP that NAV be calculated "in accordance with" the Guide has resulted in some confusion on this issue. Therefore, we suggest the Board amend this language to state that NAV be calculated in a manner that "is consistent with" the Guide.

Measurement objective

We agree with the Board's decision to define the use of unadjusted NAV in measuring the fair value of alternative investments as a practical expedient with clear disclosure of this measurement methodology. As is the case with close-end funds that currently trade on exchanges at prices that differ from NAV, we believe that many alternative investments in the scope of the proposed FSP would similarly trade at prices other than NAV per share if liquid markets for these investments existed. By clarifying that the measurement of alternative investments without readily determinable fair values at NAV per share represents a practical expedient, the Board is able to alleviate the complexities involved with identifying and quantifying factors that would cause fair values to move away from the NAV per share, without diminishing the core principle of fair value as an exit price. We believe that limiting this practical expedient to those investments within the scope of the proposed FSP, and prohibiting application by analogy to any other estimates of fair value, is appropriate for purposes of the limited objective of the proposed FSP as any widespread use of such a practical expedient would seriously undermine the fair value measurement objective.

The proposed FSP provides for a practical expedient in measuring investments within its scope when the NAV per share is determined in accordance with the Guide as of the reporting entity's measurement date. However, we urge the Board to clarify the measurement objective for alternative investments in those situations in which these specific requirements are not met. For example, in situations in which NAV is calculated as of a date that does not correspond to the reporting entity's measurement date, the proposed FSP should explicitly state whether the measurement objective is to estimate what the NAV would be as of the reporting entity's measurement date or the true exit price of the investment including potential discounts or premiums. Said differently, does the Board believe the cost and effort involved in evaluating the specific features of the investment and any related transactions is justified in situations in which NAV is not calculated as of the reporting entity's measurement date?

If the Board determines such cost and effort is justified in these situations, we believe the proposed FSP should provide additional guidance to assist reporting entities in assessing which attributes and features of the alternative investment should be

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considered when estimating fair value. Without additional guidance, constituents will struggle with the same issues that resulted in the need for the proposed FSP to begin with.

Required use of the practical expedient

We agree with the Board's decision that a reporting entity be permitted, but not required, to utilize the practical expedient. Requiring the measurement of alternative investments within the scope of the proposed FSP at their unadjusted NAV would, in our view, be a change to the measurement objective for these instruments. While we might support such an approach, because we believe a consistent measurement objective for similar instruments is an optimal solution, we do not believe it would be appropriate to make such a significant change through the issuance of an FSP that requires the use of a practical expedient. Instead, such a change would require careful consideration of the broader issue of whether fair value is the appropriate measurement for a variety of assets and liabilities that are measured at fair value today. Also, we understand the regulatory complexities that would be associated with a decision to change the measurement objectives for investments held in certain regulated entities, and as such, agree that the practical expedient provided by FASB represents the most efficient approach to address this pressing issue.

Readily determinable fair value

Investment and redemption transactions between investors and investees for certain types of alternative investments may occur at prices that differ from reported NAV per share. Investments in certain common or collective trust funds (CCTs), securities lending pools or stable value funds are examples of situations in which this may occur. Currently, there is confusion amongst constituents as to the relevance of transaction prices versus NAV in estimating the fair value of these types of investments. Constituents have also questioned what effect, if any, the guidance in the proposed FSP would have on estimating the fair value of these investments.

Some constituents question whether such investments are excluded from the scope of the proposed FSP, as they believe the prices at which investment and redemption transactions are executed represent a readily determinable fair value for these instruments (as defined in Statement 115). Others, including ourselves, do not believe the transaction price can be presumed to represent the fair value of these instruments, as many investments contain restrictions that prohibit redemption at the measurement date, and some transaction prices incorporate implicit or explicit guarantees of a specific contract amount. For example, under a CCT arrangement held by a benefit plan, plan participants can typically redeem their interests at the published unit value when receiving a distribution or making a transfer; but the plan itself must often provide a significant notice period (e.g., 12 months) prior to redemption with no assurance regarding the expected transaction price. As such, observed prices from transactions between plan participants and the investee may not be representative of the fair value of the plan's investment in the investee.

The proposed FSP does not provide any additional guidance regarding how to determine when fair value is readily determinable in these instances; instead, the proposed FSP refers to the existing guidance in paragraph 3 of Statement 115. Accordingly, we do not believe these investments would presumptively be excluded from the scope of the proposed FSP as the transaction price may not equate to an exit price between two market participants that are independent of the reporting entity (e.g., because of restrictions on redemption or credit risk associated with guarantees or past support from a party that is not obligated to provide future guarantees or support). In order to alleviate confusion and the potential for diversity in practice, we recommend that the Board provide further clarification whether these transaction prices represent readily determinable fair values.



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Disclosures

We support the incremental disclosure requirements in the proposed FSP, as they provide users of the financial statements with additional information regarding various risks associated with features of the investments that may not be captured in the NAV. However, we are concerned that insufficient guidance is provided with respect to determining the "major categories" of investments at which these disclosures need to be made. As exposed, the proposed FSP simply notes that "major category" be determined on the basis of the nature and risk of the investment. To help ensure meaningful and more consistent disclosures, we recommend the Board provide examples of factors reporting entities might consider in distinguishing the nature and risk of the investments. Alternatively, the Board could provide examples of various major categories in a manner consistent with the disclosure guidance provided in FSP FAS 157-4, Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly, and FSP FAS 132(R)-1, Employers' Disclosures about Postretirement Benefit Plan Assets.

In addition, we suggest the Board consider a requirement for reporting entities to disclose the amount of any day one gains (or losses) that were recognized as a result of applying the practical expedient. That is, disclosure should be required in situations in which a reporting entity acquires an alternative investment for an amount less than (or exceeding) reported NAV.

We would be pleased to discuss our comments with the Board members or the FASB staff at your convenience.

Very truly yours,

Ernet + Young LLP