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September 7, 2004

Ms. Suzanne Bielstein Director of Major Projects and Technical Activities Financial Accounting Standards Board 401 Merritt 7 Norwalk, CT 06856-5116

Re: File Reference No. 1201-100

Dear Sue:

Microsoft^{*}

Letter of Comment No: 6
File Reference: 1201-100
Date Received: 9-9-04

Microsoft appreciates the opportunity to respond to the Exposure Draft, "Fair Value Measurements". Given the ED indicates that the Board expects to address issues relating to the relevance and reliability of fair value measurements in subsequent phases of the fair value measurements project, we were surprised to see statements such as, "the result should be increased consistency in application and, with respect to the resulting fair value requirements, increased reliability and comparability". While we believe the guidance proposed in the ED will result in a modest increase in the consistency of application, we do not believe there is any compelling evidence provided that supports the claim of increased reliability and comparability with respect to the resulting fair value measurements. In fact, we believe a further move to fair value measurements could result in less reliable financial statements.

In addition to our concerns regarding reliability, we are not convinced that a further move to fair value measurements will result in more relevant financial reporting. In our June 2000 response to the Preliminary Views, "Reporting Financial Instruments and Certain Related Assets and Liabilities at Fair Value", we indicated that we did not believe that the FASB had provided enough compelling arguments or evidence in the Preliminary Views and that the FASB needed to do more research on how financial statement users do or could use fair value information in their work before making another critical step in the potential move from historical cost to fair value accounting. We hope you can understand our frustration when the Basis for Conclusions of the ED indicates that, "Users of financial statements generally have agreed that fair value information is relevant", but provides no evidence to support that statement, does not discuss whether fair value information is more relevant, or provides any kind of explanation for the qualifier "generally".

In addition to our concerns about the relevance and reliability of fair value measurements, we are also concerned with the cost in requiring preparers to incorporate multiple valuation techniques in Level 3 valuations and the disclosure requirements of the ED. Although there is a mention of "without undue cost and effort" in the guidance for Level

3 estimates, we are concerned with the requirement for multiple valuation techniques consistent with the market approach, income approach, and cost approach. In fact, it appears that the undue cost and effort notion only applies to whether information is available to apply multiple valuation techniques. However, it has been our experience when doing valuations, or engaging valuation specialists, that one approach may be much more relevant under the circumstances despite the fact that information is available for other approaches. The ED should not require multiple valuation techniques if one approach is much more relevant under the circumstances, regardless of whether information is available to perform other valuation techniques.

We are strongly opposed to the proposed disclosures in the ED, especially on a quarterly basis. First, we are disappointed that the Board did not use this opportunity to reevaluate all the existing fair value disclosure requirements in order to examine their relevance and to determine if or how the information is being used. Secondly, we fail to see how items such as disclosing the percentage of assets and liabilities that are based on fair value measurements and segregating those fair values between quoted prices of identical items, quoted prices of similar items, valuation models based on significant market inputs, and valuation models based on significant entity inputs are improvements in financial reporting.

The Basis for Conclusions provides the general statement that, "the disclosures required by this Statement would provide information that is useful to users of financial statements in assessing the effects of the fair value measurements used in financial reporting", but there is no mention of how the information will be useful or how it will be used. In addition, the Basis for Conclusions indicates that, "The Board believes that because the disclosures required by this Statement rely largely on the information used to develop the related fair value measurements, entities should have the information necessary to make the disclosures". Just because information is available does not mean that its disclosure will result in improved financial reporting.

Our responses to the specific issues raised in the ED are attached. If you have any questions, please contact me at (425)/703-6094.

Sincerely,

Bob Laux

Director, Technical Accounting and Reporting

Definition of Fair Value

Issue 1: This proposed Statement would define fair value as "the price at which an asset or liability could be exchanged in a current transaction between knowledgeable, unrelated willing parties" (paragraph 4). The objective of the measurement is to estimate the price for an asset or liability in the absence of an actual exchange transaction for that asset or liability. Will entities be able to consistently apply the fair value measurement objective using the guidance provided by this proposed Statement together with other applicable valuation standards and generally accepted valuation practices? If not, what additional guidance is needed? (Specific aspects of the guidance provided by this proposed Statement are considered below.)

Response: We believe the guidance in the ED will result in a modest increase in the consistency of application of fair value measurements. However, we do not believe that any amount of additional guidance could overcome the reliability issues of certain fair value measurements.

Valuation Techniques

Issue 2: This proposed Statement would clarify and incorporate the guidance in FASB Concepts Statement No. 7, Using Cash Flow Information and Present Value in Accounting Measurements, for using present value techniques to estimate fair value (Appendix A). Is that guidance sufficient? If not, what additional guidance is needed?

Response: We believe it would be more appropriate for the Board to amend Concepts Statement No. 7. Conceptual guidance for using present value techniques for fair value measurements belongs in a Concepts Statement, not a Statement of Financial Accounting Standards.

Active Markets

Issue 3: This proposed Statement would clarify that valuation techniques used to estimate fair value should emphasize market inputs, including those derived from active markets. In this proposed Statement, active markets are those in which quoted prices are readily and regularly available; readily available means that pricing information is currently accessible and regularly available means that transactions occur with sufficient frequency to provide pricing information on an ongoing basis. Is that guidance sufficient? If not, what additional guidance is needed?

Response: That guidance is sufficient.

Valuation Premise

Issue 4: This proposed Statement would provide general guidance for selecting the valuation premise that should be used for estimates of fair value. Appendix B illustrates the application of that guidance (Example 3). Is that guidance sufficient? If not, what additional guidance is needed?

Response: That guidance is sufficient and we agree that if a business is a going concern or an asset is configured for use by an entity, a going concern or in use valuation premise is appropriate.

Fair Value Hierarchy

Issue 5: This proposed Statement would establish a hierarchy for selecting the inputs that should be used in valuation techniques used to estimate fair value. Those inputs differ depending on whether assets and liabilities are identical, similar, or otherwise comparable. Appendix B provides general guidance for making those assessments (Example 4). Is that guidance sufficient? If not, what additional guidance is needed?

Response: That guidance is sufficient.

Level 1 Reference Market

Issue 6: In this proposed Statement, the Level 1 reference market is the active market to which an entity has immediate access or, if the entity has immediate access to multiple active markets, the most advantageous market. Appendix B provides general guidance for selecting the appropriate reference market (Example 5). Is that guidance sufficient? If not, what additional guidance is needed?

Response: Yes, that guidance is sufficient.

Pricing in Active Dealer Markets

Issue 7: This proposed Statement would require that the fair value of financial instruments traded in active dealer markets where bid and asked prices are more readily and regularly available than closing prices be estimated using bid prices for long positions (assets) and asked prices for short positions (liabilities), except as otherwise specified for offsetting positions. Do you agree? If not, what alternative approaches should the Board consider?

Response: Consistent with SEC ASR No. 118, we believe entitles should have flexibility in selecting the method to estimate fair value within a bid-asked spread, provided that the method is consistently applied.

Measurement of Blocks

Issue 8: For unrestricted securities with quoted prices in active markets, many FASB pronouncements (including FASB Statement No. 107, Disclosures about Fair Value of Financial Instruments) require that fair value be estimated as the product of a quoted price for an individual trading unit times the quantity held. In all cases, the unit of account is the individual trading unit. For large positions of such securities (blocks) held by broker-dealers and certain investment companies, the AICPA Audit and Accounting Guides for those industries (the Guides) permit fair value to be estimated using blockage factors (adjustments to quoted prices) in limited circumstances. In those cases, the unit of account is a block.

The Board initially decided to address that inconsistency in this proposed Statement as it relates to broker-dealers and investment companies. The Board agreed that the threshold issue is one of determining the appropriate unit of account. However, the Board disagreed on whether the appropriate unit of account is the individual trading unit (requiring the use of quoted prices) or a block (permitting the use of blockage factors). The majority of the Board believes that the appropriate unit of account is a block. However, the Board was unable to define that unit or otherwise establish a threshold criterion for determining when a block exists as a basis for using a blockage factor. The Board subsequently decided that for measurement of blocks held by broker-dealers and certain investment companies, current practice as permitted under the Guides should remain unchanged until such time as the Board fully considers those issues. For those measurements, do you agree with the Board's decision? If applicable, what approaches should the Board consider for defining a block? What, if any, additional guidance is needed for measuring a block?

Response: We believe fair value should be estimated using a blockage factor when a large block of securities is held. The Board should perform additional research on when block discounts are incurred and how the parties to the transaction determine the amount of discount.

Level 3 Estimates

Issue 9: This proposed Statement would require that in the absence of quoted prices for identical or similar assets or liabilities in active markets, fair value be estimated using multiple valuation techniques consistent with the market approach, income approach, and cost approach whenever the information necessary to apply those techniques is available without undue cost and effort (Level 3 estimates). Appendix B provides general guidance for applying multiple valuation techniques (Examples 6–8). Is that guidance sufficient? If not, what additional guidance is needed?

Response: We are concerned with the requirement for multiple valuation techniques consistent with the market approach, income approach, and cost approach. It appears that the undue cost and effort notion only applies to whether information is available to apply multiple valuation techniques. It has been our experience when doing valuations, or engaging valuation specialists, that one approach may be much more relevant under the circumstances despite the fact that information is available for other approaches. The ED should not require multiple valuation techniques if one approach is much more relevant under the circumstances, regardless of whether information is available to perform other valuation techniques.

Restricted Securities

Issue 10: This proposed Statement would require that the fair value of restricted securities be estimated using the quoted price of an otherwise identical unrestricted security, adjusted for the effect of the restriction. Appendix B provides general guidance for developing those estimates, which incorporates the relevant guidance in SEC ASR No.

113, Statement Regarding "Restricted Securities." Is that guidance sufficient? If not, what additional guidance is needed?

Response: We agree that the fair value of restricted securities should be adjusted for the effect of the restriction and that the guidance provided is sufficient.

Fair Value Disclosures

Issue 11: This proposed Statement would require expanded disclosures about the use of fair value to remeasure assets and liabilities recognized in the statement of financial position. Appendix B illustrates those disclosures. This proposed Statement also would encourage disclosures about other similar remeasurements that, like fair value, represent current amounts. The Board concluded that those disclosures would improve the quality of information provided to users of financial statements. Do you agree? If not, why not?

Response: No, we fail to see how items such as disclosing the percentage of assets and liabilities that are based on fair value measurements and segregating those fair values between quoted prices of identical items, quoted prices of similar items, valuation models based on significant market inputs, and valuation models based on significant entity inputs are improvements in financial reporting. The Basis for Conclusions provides the general statement, "the disclosures required by this Statement would provide information that is useful to users of financial statements in assessing the effects of the fair value measurements used in financial reporting", but there is no mention of how the information will be useful or how it will be used. In addition, the Basis for Conclusions indicates that, "The Board believes that because the disclosures required by this Statement rely largely on the information used to develop the related fair value measurements, entities should have the information necessary to make the disclosures". Just because information is available does not mean that its disclosure will result in improved financial reporting. Also, we are disappointed that the Board did not use this opportunity to reevaluate all the existing fair value disclosure requirements in order to examine their relevance and to determine if or how the information is being used.

Effective Date

Issue 12: This proposed Statement would be effective for financial statements issued for fiscal years beginning after June 15, 2005, and interim periods within those fiscal years. The Board believes that the effective date provides sufficient time for entities to make the changes necessary to implement this proposed Statement. Do you agree? If not, please explain the types of changes that would be required and indicate the additional time that would be needed to make those changes.

Response: We agree.

Other Issues

Issue 13: This proposed Statement represents the completion of the initial phase of this project. In subsequent phases, the Board expects to address other issues, including issues relating to the relevance and reliability of fair value measurements and the unit of

account that should be used for those measurements. What, if any, other issues should the Board address? How should the Board prioritize those issues?

Response: These should be top priorities for the Board as we continue to have concerns about the relevance and reliability of fair value measurements.

Public Roundtable Meeting

Issue 14: The Board plans to hold a public roundtable meeting with respondents to the Exposure Draft on September 21, 2004, at the FASB offices in Norwalk. Please indicate whether you are interested in participating in the meeting. If so, comments should be submitted before that meeting.

Response: We would be interested in participating in the public roundtable meeting.