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Financial Accounting Standards Board
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Gentlemen:

This letter is in response to your exposure draft, "Accounting Changes and Error Corrections." Two items especially caught my attention: retroactivity and extraordinary transactions.

Retroactivity

When I first glanced at the text of this exposure draft and saw retrospective application, I was horrified. As a financial officer in an organization established on September 27, 1540, I felt it would be impossible to implement this. After a more careful reading, I realized that retroactivity in this exposure draft is not quite as burdensome as it could at first seem because of the exceptions to the requirement. In my experience, it is quite difficult to put oneself in the position of a decision maker even ten years ago while removing the benefit of hindsight. I believe you should anticipate a headlong rush to the exceptions section of the standard in paragraph 11. This result will often, in my view, limit retroactivity to statements shown and—maybe—a few other years.

I do not intend this as a negative comment on the exceptions. On the contrary, I think recognizing exceptions is the only realistic approach to take in looking at long-established organizations possibly even hundreds of years old. Since the draft is part of an international convergence effort, I recommend that you not yield on the exceptions unless you broaden them. Opinion 20, I believe, was oriented to practicality even at the cost of some prior-period comparability. Tightening the exceptions any further could, I fear, reverse the practicality of Opinion 20.

Extraordinary Transactions

Another item surprised me. That is your description in paragraphs 20 and B7 of certain transactions as extraordinary. This term is not out of order in the United States. But elsewhere it can lead to great confusion. Let me explain.

For over twenty years I have been a financial consultant or an internal auditor for numerous organizations in the

Catholic Church. In these capacities, I have had occasion to visit many entities in Africa, Asia, Europe, Central America, and the United States. There are, of course, quite a few variations in how accounting is done in all of these places. Your goal in the convergence project is to eliminate or at least reduce these variations. With that I am in full accord. The sooner convergence takes place, the better.

One of the accounting systems I have encountered rests on a distinction between ordinary and extraordinary transactions. I have seen remnants of this system in continental Europe, where it originated, and the full system in Africa and Asia.

Under this ordinary/extraordinary system, ordinary transactions correspond fairly well with what US GAAP would regard as routine annual business. But extraordinary transactions cause one violation of GAAP after another. The purchase of an office building, for example, would be treated in a special category of annual expenses, i.e., extraordinary, but at the end of the year that category would be closed to the same equity account as the ordinary operations. Since the entire cost is charged at acquisition, depreciation does not fit in the system. The statement of financial position nowhere explicitly reflects a fixed asset; instead the equity account is diminished by the full acquisition cost in year 1. There does not have to be a note listing the fixed assets owned—although sometimes there is. Consequently, statements of financial position are statements of liquid assets, liabilities, and (diminished) equity.

Readers of business and/or non-profit reports produced in this system could easily be misled if they were not well versed in both the accrual and the ordinary/extraordinary systems. I have dealt with that system in some church organizations. I have also met business executives who were furious at European business partners whose statements did not report fixed assets and their accumulated depreciation. What had appeared to be a strong cash position at the partner firm proved to be the exact opposite.

Because of the international import of the convergence project, I suggest that FASB, either here or in some other document (perhaps a revision of a concepts statement), reject accounting systems based on a distinction between ordinary and extraordinary transactions. About two years ago, an IASB draft proposed the rejection of this concept of extraordinary transactions. I wrote a comment letter on that document and supported the IASB stance.

I may be making too much out of this issue of extraordinary transactions. Those who wrote the present exposure draft may never have heard of a system based on ordinary and extraordinary transactions. I am sure they have never had to deal with accountants who are vehement proponents of, or survivors of, such systems.

If I can be of any further assistance on this matter, please do not hesitate to contact me.

Very truly yours,

Henry T. Chamberlain, S.J.

Postscript

Your calendar as of January, 2004, indicates that your exposure draft on combinations of not-for-profit organizations has now been postponed at least twice. It is currently listed for an exposure draft in the third quarter of this year, with a final version in the first quarter of 2005.

It would be very helpful in my work if you would not postpone this topic again. Because many associations of non-profit organizations may wish to convene meetings after the exposure draft comes out, I hope you will give it a comment period of 60 days or more. In the non-profit world, a shorter comment period often may not give enough time for associations to convene meetings. (Not all non-profit associations have standing committees on accounting.) I would be very pleased if I could download this exposure draft from your web site around September 20, 2004.

Thank you for your consideration.