



Centre for  
Financial  
Market  
Integrity



LETTER OF COMMENT NO. 6

13 June 2008

Mr. Russell G. Golden  
Director of Technical Application and Implementation Activities  
Financial Accounting Standards Board  
401 Merritt 7  
PO Box 5116  
Norwalk, CT 06856-5116

**Re: File Reference: Proposed FSP ARB 43-a**

Dear Mr. Golden:

The CFA Institute Centre for Financial Market Integrity (CFA Institute Centre),<sup>1</sup> in consultation with its Corporate Disclosure Policy Council (CDPC)<sup>2</sup>, appreciates the opportunity to comment on the Financial Accounting Standards Board (FASB) Staff Position ARB 43-a (the “FSP”).

The CFA Institute Centre represents the views of its investment professional members, including portfolio managers, investment analysts, and advisors, worldwide. Central tenets of the CFA Institute Centre mission are to promote fair and transparent global capital markets, and to advocate for investor protections. An integral part of our efforts toward meeting those goals is ensuring that the quality of corporate financial reporting and disclosures provided to investors and other end users is of high quality. The CFA Institute Centre also develops, promulgates, and maintains guidelines encouraging the highest ethical standards for the global investment community through standards such as the *CFA Institute Code of Ethics and Standards of Professional Conduct*.

### **Introduction**

The CFA Institute Centre supports the proposals within the FSP as they call for the increased use of fair value measurements. As noted in previous comments to the FASB, we hold the belief that

---

<sup>1</sup> The CFA Institute Centre for Financial Market Integrity is part of CFA Institute. With headquarters in Charlottesville, VA, and regional offices in New York, Hong Kong, and London, CFA Institute is a global, not-for-profit professional association of more than 95,000 investment analysts, portfolio managers, investment advisors, and other investment professionals in 134 countries, of whom nearly 82,000 hold the Chartered Financial Analyst® (CFA®) designation. The CFA Institute membership also includes 135 member societies in 56 countries and territories.

<sup>2</sup> The objective of the CDPC is to foster the integrity of financial markets through its efforts to address issues affecting the quality of financial reporting and disclosure worldwide. The Council is comprised of investment professionals with extensive expertise and experience in the global capital markets, some of whom are also CFA Institute member volunteers. In this capacity, the Council provides the practitioners’ perspective in the promotion of high-quality financial reporting and disclosures that meet the needs of investors.

Re: FSP ARB 43-a  
13 June 2008  
Page 2

fair value information is the most relevant information for financial decision making<sup>3</sup>. These changes offer improvements to all types of investors and users of the financial reports.

Our long-term goals include the use of fair value measurements for all assets and liabilities. We support the stated notion of fair value being the most relevant to trading activities and the potential benefits it brings to financial reporting described in the FSP's summary on page 5. To continue the transition of financial reporting to use a greater level of fair value measurements, we understand the journey is best completed through the undertaking of defined and measured steps as offered with this proposal.

The remainder of our letter addresses several issues the board considered; as well as our request for increasing the level of required disclosures.

#### **Issue 1: Commodity Inventories**

We agree with FASB's decision to reject the alternative of limiting the scope of the FSP based on the use of the inventory item. As mentioned above, we favor the broader application of fair value measurements within financial reporting. This alternative could allow the intent of management to create different accounting treatments for comparable inventory items.

#### **Issue 2: Readily Determinable Fair Value**

We agree with FASB's decision to reject the alternative of limiting the scope of the FSP based on the availability of "*readily determinable fair values*". As is noted, this alternative would create inconsistencies with other accounting standards. The relevance of information to making investment decisions is independent of its reliability. Concerns about reliability can be alleviated by adequate disclosure.

#### **Issue 3: Trading Items Other Than Physical Inventories**

As the FASB contemplates the increased use of fair value measurements, it consistently finds other comparable areas to consider. While we hold the long-term view of using fair value measurements for the entirety of financial reports, expanding the scope of this project is not necessary. This FSP represents one of the many steps along the path to fair value and should not be delayed by expanding the scope.

#### **Issue 4: Accounting Policy Election**

We agree with FASB's decision to reject the alternative of allowing an entity-wide election of inventory accounting policies. In principle, we oppose the availability of options that permit preparers to choose among alternative accounting treatments for identical transactions. We support FASB's statement "that fair value is always the appropriate measurement attribute for inventories included in trading activities".<sup>4</sup>

---

<sup>3</sup> The importance of fair value represents Principle 3 in the CFA Institute Centre's "*A Comprehensive Business Reporting Model: Financial Reporting for Investors*" (July 2007). This publication is available on the CFA Institute Centre website: <http://www.cfapubs.org/doi/pdf/10.2469/ceb.v2007.n6.4818>

<sup>4</sup> Page 3 of FASB's Proposed FSP on ARB 43 (ARB 43-a)

Re: FSP ARB 43-a  
13 June 2008  
Page 3

### **Need for Additional Disclosures**

The CFA Institute Centre supports the required disclosures presented in paragraph 11 of the FSP. These disclosures as a whole, and especially the disclosure of the typical holding period of the items, provide information useful to investors in gauging a company's risk exposures. The amounts of trading inventory and its holding periods can vary for numerous factors, and investors would be well served to have these factors discussed in sufficient detail to understand their influence. This is particularly the case when the trading inventory is an element of operations, as we discuss in the following paragraphs.

While we support the proposals included in the FSP, we do not believe it goes far enough in requiring the disclosures needed by investors. Statement of Financial Accounting Standards (SFAS) No. 161 requires the disclosure of "(a) the location and fair value of derivative instruments in the statement of financial position and (b) the location and amount of gains and losses on derivative instruments in the statement of financial performance"<sup>5</sup>. We believe that, as a minimum, this level of information should be provided for trading inventories measured at fair value.

We propose adding the following items to Statement 9 of ARB 43:

- e. Trading inventory, that is inventory carried at fair value, should be presented as a separate line item in the balance sheet or parenthetically disclosed on the face of the balance sheet as to the amount of inventory carried at fair value.
- f. Changes in fair value recorded from marking inventory to fair value during the period should be disclosed on a separate line item in the income statement or separately disclosed in the notes.

Paragraph A35 of SFAS No. 161 discusses the modification to the tabular disclosure for derivative instruments not designated or qualifying as hedging instruments if the entity's policy is to include those derivative instruments in its trading activities; paragraphs 44C(c)(1) through (3) identify the disclosures for those derivatives that must be provided instead. We note that the alternative disclosures illustrated in SFAS No. 161 for derivative instruments that are included in an entity's trading account aggregate the gains and losses on both derivative and nonderivative instruments. We believe that the amount of the gains and losses associated with carrying inventory in the trading account at fair value should be separately disclosed from the derivative gains and losses. We are requesting this disclosure because we do not expect that the guidance of this FSP will be limited to investment companies or broker dealers. For example, there are companies with agricultural operations that carry over 50% of their inventory at fair value. As we understand it, if those companies continue to carry their agricultural inventory at fair value the inventory will need to be considered trading inventory.

---

<sup>5</sup> Paragraph A25 in SFAS No. 161 *Disclosures about Derivative Instruments and Hedging Activities*

Re: FSP ARB 43-a  
13 June 2008  
Page 4

It is essential that investors be able to differentiate the earnings streams generated by the conventional conversion of inventory into finished goods and sales from those due to changes in market prices. When derivatives are used to hedge those agricultural positions, we need to differentiate the change in value of operational assets from the changes in value of contracts electively entered into to modify the risk structure of the entity. In other words, we need to see the effect of hedging transactions separately from the fair value changes in the underlying in order to understand the scope and effect of those transactions.

**Conclusion**

The proposed FSP represents a positive change to financial reporting for the users of financial reports. Our request for additional required disclosures should not create significant delays in finalizing the FSP and is consistent with other related standards.

We appreciate the opportunity to provide comments to FASB and its staff regarding FSP ARB 43-a. If any party should have questions or seek further elaboration of our views, please contact Glenn Doggett, CFA, by phone at 434.951.5278 or by e-mail at [glenn.doggett@cfainstitute.org](mailto:glenn.doggett@cfainstitute.org).

Sincerely,

*/s/Kurt N. Schacht*

Kurt N. Schacht, CFA  
Managing Director

*/s/ Gerald I. White*

Gerald I. White, CFA  
Chair, Corporate Disclosure Policy Council

cc: Corporate Disclosure Policy Council