October 28, 2005

Technical Director
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

By email to: director@fash.org

Re: File Reference No. 1204-001

Director:

First Horizon National Corporation appreciates the opportunity to comment on the Exposure Draft for the Proposed Statement of Financial Accounting Standards, Business Combinations, a replacement of FASB Statement No. 141 (the "Exposure Draft"). We believe that as proposed, the Exposure Draft presents a theoretical model of accounting for business combinations that would result in overt financial reporting inconsistencies and extremely judgmental valuation estimates. Further, we believe that the Exposure Draft's proposed requirements would pose significant difficulties for both preparers and users of financial statements by triggering highly complex post-acquisition valuation practices which would create significant earnings volatility rather than including such revisions in the price of the business acquired. Accordingly, we believe that the Exposure Draft would result in financial reporting that is less representationally faithful than the current cost accumulation model presented in Statement of Financial Accounting Standards No. 141, Business Combinations. Our concerns are more specifically presented in the following categories:

- Fair Value Accounting Model
- Direct Costs of Acquisition
- Planned Restructuring Activities
- Contingent Consideration
- Contingent Assets and Liabilities
- Valuation Allowances
- Measurement Period
- Acquisition Measurement Date
- Measurement of Equity Securities
- Disclosures
- Effective Date

Fair Value Accounting Model

Fair value accounting works well for most financial assets and liabilities because they have a fair value established in open markets. However, when fair value accounting is applied to
non-financial assets and liabilities, its ability to provide reliable financial information is significantly degraded. We acknowledge that the FASB has issued an Exposure Draft entitled *Fair Value Measurements* that attempts to provide guidance on the processes that should be used to derive fair values. However, that standard does not resolve the lack of representational faithfulness that is the result of a non-market based valuation. Simply put, in situations where similar market instruments do not exist, most fair value estimates require the application of so much judgment that they are at risk of being less reliable than reasonable approximations of fair value.

Requiring fair value accounting for acquisitions is very concerning because it will create internal inconsistencies within an acquirer’s financial statements. The Exposure Draft will also significantly reduce comparability of financial information between acquisitive and non-acquisitive companies. As will be described in more detail below, the lack of accounting consistency resulting from the Exposure Draft (if approved in its current form), will prove extremely difficult for preparers to implement and users to understand. This will primarily occur because two classes of assets and liabilities (acquired and not acquired) will be created, each requiring separate accounting methodologies which then must be communicated to investors so they understand the differences between the two classes and how earnings are affected in a volatile manner by one class (acquired) but not necessarily the other class (not acquired). Accordingly, we believe that if the fair value model is implemented for acquisitions, disparate treatment of similar items within an acquirer’s financial statements as well as the resulting comparative financial statement inconsistencies between issuers could, over time, become significant enough to risk rendering large portions of financial information and associated analysis meaningless.

We further believe that the cost accumulation model of accounting for acquisitions has worked well because it is more representationally faithful to the concept of opportunity cost, wherein assets are allocated to implement particular strategies based on an expected return and all expenditures necessary to achieve a particular strategy must be included to appropriately determine its expected return. By creating assets and liabilities that are not even probable at the time of acquisition and subsequently requiring those assets and liabilities to be remeasured through earnings until ultimate resolution, accounting for acquisitions under the provisions of the Exposure Draft would distort actual returns on the acquired business.

**Direct Costs of Acquisition**

Consistent with our views on the existing cost accumulation model of accounting for acquisitions, we disagree with the requirements of paragraphs 27 and 1397 of the Exposure Draft, and we believe that the direct costs of acquiring another business should be considered part of the purchase price of that business. Such expenditures would not be incurred unless they were necessary to complete the acquisition transaction. Requiring their inclusion within earnings distorts reported amounts of net income because those costs would not have been incurred unless the acquisition was completed. As such, those expenditures should be considered part of the cost of the business acquired.

**Planned Restructuring Activities**

The requirements of paragraph 35 to consider post-combination restructuring activities as period expenses (even if the restructuring is contemplated at the time of acquisition) fails to recognize that acquirers contemplate a restructuring of the acquiree’s operations at the time
of acquisition. Consistent with our support for the cost accumulation model, we believe that if management substantiates its assertion that a restructuring was contemplated at the time of acquisition, such expenditures should be considered part of the price of the business acquired. Therefore, we believe the concepts underlying Emerging Issues Task Force Issue No. 95-3, Recognition of Liabilities in Connection with a Purchase Business Combination should continue to apply in determining the price paid in an acquisition.

**Contingent Consideration**

Paragraphs 25 and 26 of the Exposure Draft indicate that the fair value of contingent consideration is to be estimated at the acquisition date and subsequently adjusted through earnings until resolution. In our experience, contingent consideration often takes the form of a deferral of up front purchase price until a specified future event or earnings level is achieved. In these circumstances, the acquirer withholds a portion of the purchase price to ensure that an appropriate transition is completed. Requiring an estimate of the amounts to be paid at acquisition date presents management with a complex valuation process that will almost certainly result in an amount that is different than what is ultimately paid in consideration for the acquired business. Requiring such differences to be included within period earnings distorts the actual price paid to complete the acquisition of the acquirer's operations. Consistent with our views on the cost accumulation model, we believe that all amounts paid to sellers in conjunction with an acquisition should be considered part of the purchase price regardless of when paid.

**Contingent Assets and Liabilities**

The requirements of paragraph 35 to estimate the fair value of contingencies at the acquisition date and recognize future changes in fair value through earnings will result in a direct inconsistency with the current treatment of an acquirer's own contingencies, effectively creating disparate accounting treatments for two classes of contingencies on the acquirer's balance sheet post-acquisition. Acquired contingencies will be recognized at fair value with probability included as a component of the valuation of the asset or liability. Contingencies that are not acquired will continue to follow the guidance of Statement of Financial Accounting Standards No. 5, Accounting for Contingencies ("SFAS No. 5") and FASB Interpretation No. 14, Reasonable Estimation of the Amount of a Loss with recognition dependent upon an assessment of probability. The fallacy of this inconsistency is best highlighted when considering an industry-wide litigation exposure that is not probable of resulting in a loss. In accordance with SFAS No. 5, an acquirer would not recognize its own exposure to the liability within its financial statements and should consider an appropriate disclosure. However, the acquirer must assign a probability and recognize the liability as part of its accounting for the purchase of a business exposed to the same litigation risk. Further, the acquired liability will be marked to fair value each reporting period until it is resolved. This process results in a litigation accrual of limited relevance because it does not reflect the acquirer's complete risk exposure, nor does it represent a liability that is probable of being incurred.

We also feel that additional clarification needs to be provided for situations where a contingent asset exists. For example, when an acquirer advances a portion of the purchase price to the sellers, but a clawback provision exists. As currently written, we believe paragraph 35 indicates that such contractual rights would represent a contingent asset to be accrued as part of the acquisition. Gain contingencies of this nature would be strictly prohibited for accrual under SFAS No. 5. However, the Exposure Draft appears to require their recognition as part of the allocation of purchase price.
Valuation Allowances

Paragraph 34 of the Exposure Draft prohibits the carryover of valuation allowances for loans acquired in a business combination. Despite the existence of AICPA Statement of Position 03-3, Accounting for Certain Loans or Debt Securities Acquired in a Transfer ("SOP 03-3") we continue to object to this treatment. The SEC established the parameters for allowance carryover in SEC Staff Accounting Bulletin No. 61, Adjustments to Allowances for Loan Losses in Connection with Business Combinations ("SAB No. 61") and we believe that SAB No. 61 represents sufficient guidance to insure that allowances are not artificially increased as part of a business combination. Further, when discussing the requirements of SOP 03-3, we were flatly rejected by two software vendors who indicated that the accetable/non-accetable yield accounting requirements discussed therein were "accounting" issues and not loan servicing issues. We believe that this was done because of the magnitude of changes required to their software to incorporate the requirements of SOP 03-3. Making a similar requirement for all acquired loans would exceed the capability of "spreadsheet" accounting and therefore would require significant time and effort to implement. Additionally, prohibiting the carryover of loan reserves will result in a portion of credit risk being embedded within a loan discount that will ultimately be accreted back to earnings through interest income. This will result in a potentially significant distortion of key financial metrics for banks (e.g., coverage ratio and net interest margin) which is caused by the differentiation between acquired and non-acquired assets.

Measurement Period

The requirement of paragraph 67 of the Exposure Draft to retroactively apply changes to the initial estimates if future events reflect upon the values of assets and/or liabilities at that time would result in unnecessary revisions to prior financial statement information which could only result in increased confusion for investors. This requirement is also inconsistent with the complex valuations that will be required of management in preparing fair value measurements. Today it is not uncommon for valuations to take up to six months after acquisition to appropriately value all elements of an acquired business. When the complexity of fair value measurements for contingencies are added, this time period could easily extend up to one year. Mandating that all previously reported periods must be adjusted when the valuations are finalized would cause multiple periods of previously released financial information to be revised, effectively punishing public companies for unavoidable and necessary delays in completion of normal valuation processes. We believe that retrospective application should be voluntary with required disclosure of the method elected.

Acquisition Measurement Date

Paragraph B54 indicates that the designation of a transaction's effective date will no longer be acceptable. While we agree that designation of an effective date is not conceptually preferable, in many cases designation of a date that is at the beginning or end of a month, particularly in situations where an announcement has occurred prior to the specified date, is done solely to facilitate accounting for the pre- and post-combination operating periods. Designating effective dates at the end or beginning of a month greatly improves the efficiency of accounting for acquisitions by allowing businesses to perform their normal "close the books" processes and use such amounts to terminate the operations of the seller and initiate control by the acquirer.
Measurement of Equity Securities

Paragraph 21 requires that equity instruments issued in the acquisition should be measured as of the acquisition (normally closing) date. We believe that this requirement is inconsistent with valuing an acquisition based on the agreement between the parties. In situations where the parties to a transaction agree on the method of valuing equity securities to be transferred to the sellers, that method should be used to determine the value of equities ultimately transferred. Requiring the valuation of equity securities as of the closing date detracts the measurement of fair value exchanged from the contractual basis for the acquisition, resulting in financial reporting that is less representative of the parties' intent. Therefore, we strongly disagree with the requirement to use the acquisition date to measure the value of equity securities delivered to sellers in an acquisition.

Disclosures

We believe that the disclosure requirements of paragraphs 71 through 81 contain a number of items that are of limited relevance to the financial statements. Paragraph 72(d) requires disclosure of the primary reasons for the business combination including a description of factors that resulted in the recognition of goodwill. We do not believe that such information should be required in a GAAP presentation of financial information. The primary reasons for a business combination, as well as a justification of price paid, are more appropriately addressed by management within a press release announcing the transaction or in management's discussion and analysis ("MD&A") for public registrants.

Paragraph 72(h) indicates that the maximum amount of contingent payments should be disclosed. This seems contradictory to the requirement of paragraphs 25 and 26 to initially recognize such amounts at fair value and include all subsequent changes in fair value through current earnings. Once management has made its estimate of the fair value of such payments, why should the aggregate amount of contingent consideration require disclosure? Differences in the amounts ultimately paid and the initial estimate will be included in earnings (if not classified as equity) under the requirements of paragraph 26. Differences in equity securities ultimately issued would be included in the equity rollforward. If actual cash amounts paid differ materially from estimates, the changes should be disclosed in the period in which earnings are impacted as part of MD&A if not sufficient to warrant a separate financial statement line item.

Similarly, the requirement of Paragraph 72(i) to disclose aggregate costs incurred in connection with a business combination is wholly inconsistent with the requirements of paragraph 27 to expense such costs. Disclosure would be relevant if such expenditures were included within goodwill as a component of purchase price, but requiring their disclosure when expensed contradicts the consideration of these expenditures as a period expense. Such costs should be addressed within MD&A if not sufficient to warrant a separate financial statement line item.

Paragraph 74(a) requires the disclosure of revenues and net income of the acquiree for periods subsequent to the acquisition date. We must note that consistent with the discussion in paragraph B138, identifying post-acquisition revenues and net income attributable to the acquired business can be very difficult, if not impossible, once the acquiree has been integrated within the acquirer's operations, which is necessary to experience many of the synergies expected after acquisition. Further, this requirement fails to address how such synergies should be addressed within the disclosure. Are synergies to be presented within
the ongoing operations of the acquiree? Should synergies be shown separately in a pro forma presentation?

Additionally, paragraph 74(b) retains the requirement to provide pro forma disclosure of the results of operations for the combined entity for the current reporting period and corresponding period from the prior year as if the acquisition occurred at the beginning of each respective fiscal year. We believe that this is duplicative of the pro forma disclosure of ongoing operations of the acquiree. Each presentation strives to provide investors with a measure of the effects the acquisition will have on future earnings. We believe that the FASB should select one of these two disclosures for the footnotes, preferably retaining the existing pro forma disclosures.

Paragraph 76(a)'s requirement to present a rollforward of contingencies associated with a business combination is not consistent with the requirement that post-acquisition changes in fair value should be recognized within period earnings. Consistent with our views for disclosure of the expense amounts per paragraph 72, we believe that changes in fair value of contingencies are more appropriately presented in MD&A rather than within the footnotes if not sufficient to warrant a separate financial statement line item. Should this requirement be retained in the final standard, we believe that additional clarification should be provided regarding whether all contingencies associated with an acquisition should be presented in a net manner or whether contingent assets and liabilities should be presented separately.

**Effective Date**

We strongly agree with the prospective only transition discussed in paragraph 82. However, given the dramatic changes being proposed for acquisition accounting, we believe that it will take a significant amount of time and effort after the issuance of a final standard to design, document, test and implement the necessary changes to the control environment (especially changes in loan servicing systems) that will be required to achieve compliance with the new standard. Accordingly, we believe that an effective date for fiscal years beginning after December 15, 2006, does not provide adequate time for all adoption procedures to be completed if an extended re-deliberation of the Exposure Draft occurs. We believe that it will take at least one year from the issuance of a final standard to adopt the fair value methodologies as currently proposed. Therefore, we request that the FASB provide an effective date that is at least one year after the issuance of a final standard that includes a fair value standard for valuation of acquisitions.

If you have any questions or comments regarding the comments presented in this letter, please contact me at (901) 537-1937.

Sincerely,

/ls/ Shawn P. Luke

Shawn P. Luke
Senior Manager-Accounting Research
Corporate Controller's Division
First Horizon National Corporation