United Technologies Corporation (UTC) welcomes the opportunity to share its views on the proposed FASB Staff Position “Accounting for Assets Acquired and Liabilities Assumed in a Business Combination That Arise from Contingencies” (the proposed FSP). UTC is a $60 billion global provider of high technology products and services to the building systems and aerospace industries, operating in 186 countries around the world.

We agree that clarifying guidance is required with respect to accounting for acquired contingencies and the subsequent accounting for those contingencies. We have attached our answers to the questions in the proposed FSP in Attachment A to this letter.

In summary, we believe the decision to go back to a model similar to that used in FASB Statement No. 141 “Business Combinations” (SFAS 141) is appropriate. We believe, however, that there should only be one model for recognition and subsequent accounting for contingencies. The proposed FSP appears to call for diverse accounting methodologies to be applied for different groups of contingent assets and liabilities, as follows:

1. Those that arise in our operations and acquisitions prior to January 1, 2009 - record under FASB Statement No. 5 “Accounting for Contingencies” (SFAS 5);
2. Those we acquire and record at fair value pursuant to SFAS 141(R);
3. Those we acquire and initially record at fair value pursuant to SFAS 141(R) until new information becomes available; then we subsequently account for them for under SFAS 5 and FASB Interpretation 14 “Reasonable Estimation of the Amount of a Loss” (Interpretation 14); and
4. Those that we acquire where fair value could not be initially determined pursuant to SFAS 141(R) and therefore we record at estimated future settlement and subsequently account for under SFAS 5 and Interpretation 14.
We believe the different accounting methodologies for these groups of contingencies will not only be administratively burdensome for preparers to adhere but, more importantly, too complex for readers of financial statements to understand.

We agree with the elimination of the distinction between contractual and non-contractual contingent liabilities as it is often difficult to distinguish between a contractual and non-contractual obligation.

We thank the Board for its consideration of our views and would be pleased to discuss these issues in more detail with the Board members or the FASB staff at your convenience.

Sincerely,

Margaret M. Smyth
Vice President, Controller
United Technologies Corporation
1. Will the proposed FSP meet the project’s objective to improve financial reporting by addressing application issues identified by preparers, auditors, and members of the legal profession about Statement 141(R) related to the initial recognition and measurement, subsequent measurement and accounting, and disclosure of assets and liabilities arising from contingencies in a business combination? Do you believe the amendments to Statement 141(R) in the proposed FSP are necessary, or do you believe the current requirements in Statement 141(R) should be retained?

Although we believe that some practice issues will be alleviated with the proposed FSP other practice issues will be created. For example, we believe that removing the distinction and different levels for recording contractual versus non-contractual contingencies will alleviate practice issues caused by the SFAS 141(R) model. However, we believe replacing the SFAS 141(R) requirement of recording at fair value with two different models to initially record and subsequently account for contingencies is too complex for issuers and readers. We believe that the model under the original SFAS 141 is the most appropriate one for accounting for acquired contingencies. Subsequent accounting of a contingency should then follow SFAS 5 and Interpretation 14 as outlined in the proposed FSP.

If the Board decides to allow the model as outlined in the proposed FSP, we would recommend the Board provide more examples of how to determine the fair value of contingencies related to pending or anticipated claims and litigation. From our interpretation of the model, certain acquired litigation contingencies that are currently recorded at the low end of the range under the current model (SFAS 5 and Interpretation 14) would be recorded at the midpoint of the range under this proposed FSP (if no point within a range is more probable than any other). If this is what the Board intended with this guidance it should say so expressly. Examples that would provide useful information to preparers include variations on Example 1 in the FSP. Consider, for instance, the same facts as in Example 1, except that discovery has been completed and a jury trial is scheduled for 4QX9. TC’s counsel has advised TC’s management that a jury is likely to award some damages. The range is $100,000 to $1,000,000. No amount within this range is a better estimate than any other amount. Under Statement 5 and Interpretation 14, AC would recognize a liability of $100,000 at the acquisition date. Is it the intent of the FSP that AC would have sufficient information to reasonably determine fair value and would recognize a loss of $533,333 (the mid point in the range – all points in the range are equally probable)?

An example such as this would help interpret the language in the proposed FSP as it relates to contingencies arising from pending or anticipated claims and litigation.

2. In developing this proposed FSP, the Board decided to adopt a model that is similar to the requirements in FASB Statement No. 141, Business Combinations. However, the Board decided to provide additional guidance for assessing whether the fair value of an asset or liability arising from a contingency can be reasonably
determined. Additionally, the Board decided to provide subsequent accounting guidance for assets or liabilities arising from contingencies initially recognized at fair value, which was not provided in Statement 141. Do you agree with the Board's decision to provide this additional guidance, or do you believe the proposed FSP should carry forward the requirements in Statement 141 without reconsideration, including not addressing subsequent measurement and accounting? Alternatively, do you believe the proposed FSP should require that the initial and subsequent measurement of assets and liabilities arising from contingencies in a business combination be on the same basis (that is, assets and liabilities arising from contingencies initially recognized at fair value should subsequently be remeasured at fair value)?

We believe the proposed FSP adequately addresses subsequent measurement. As we state above, we are concerned with the FSP's apparent endorsement of two different models to account for acquired contingencies. We do not agree with the fair value model of accounting for acquired contingencies. We believe all contingencies should be accounted for pursuant to SFAS 5.

3. What costs do you expect to incur or not incur if the Board were to issue this proposed FSP in its current form as a final FSP? How could the Board further reduce the costs of applying the requirements without significantly reducing the benefits?

Right now, we are uncertain about the costs we will incur as a result of adopting the proposed FSP in its current form. We believe the FSP makes accounting for acquired contingencies under SFAS 141(R) less burdensome in some respects, but then provides further complexity in reporting and subsequent accounting and measurement that didn’t exist before. We believe this complexity will result in confusion by preparers and readers of the financial statements. We believe the Board should allow acquired contingencies to be accounted for pursuant to SFAS 5, so that one standard exists for valuing contingencies.

4. This proposed FSP includes guidance for assessing when the fair value of an asset or liability arising from a contingency in a business combination can be reasonably determined. Do you believe the guidance in paragraphs 10–13 provides clear guidance for assessing when fair value can be reasonably determined? If not, please explain what additional guidance is necessary.

No, we do not believe the guidance in paragraphs 10-13 provides clear guidance for assessing when fair value can be reasonably determined, especially as it relates to contingencies arising out of pending or anticipated claims and litigation, as previously discussed. We believe additional guidance, as it specifically relates to these types of contingencies is needed, either in the form of examples, as outlined in our response to Question #1, or additional specific guidance. Without this additional guidance, we are concerned that there will be inconsistent application of what is or isn’t “reasonably determined,” specifically as it relates to these types of contingencies.
5. Constituents have raised concerns about liabilities arising from contingencies being recorded indefinitely when there is no clear resolution of the contingency because the acquirer does not believe settlement will ever be required and the liability is not subject to cancellation or expiration. Will the proposed amendment to Statement 141(R) that allows for the derecognition of a liability arising from a contingency when new information is obtained that indicates it has become remote that the obligation will be enforced address these concerns? Do you believe this guidance is operational?

Yes, we believe the guidance in this FSP addresses derecognition concerns of a liability where settlement may never be required and the liability is not subject to cancellation or expiration. However, as discussed above, we believe two models for accounting for acquired contingencies is not appropriate.

6. Although not clear, the Board did not intend the subsequent measurement and accounting guidance in Statement 141(R) to require that a liability arising from a contingency be recorded at its acquisition-date fair value until the contingency is completely resolved in cases where the acquirer is released from risk over time or the acquirer fulfills its performance obligation over time. Do you believe the clarifying guidance included in this proposed FSP is operational for the subsequent measurement and accounting of a liability initially recognized at fair value?

As discussed previously, we are concerned that there are now two models that will exist for recording contingent liabilities and subsequent remeasurement. Therefore, entities must track three different kinds of contingencies related to acquisitions (acquired measured at fair value, acquired measured at future settlement and acquired initially measured at fair value and due to new information becoming available, now under SFAS 5 and Interpretation 14) and report them based on what model they were recorded under on the acquisition date. This will be complex from a preparer standpoint and may be confusing to readers of financial statements.

7. Constituents have raised concerns about disclosing potentially prejudicial information in financial statements. Do you believe the revised disclosure requirements in this proposed FSP sufficiently protect sensitive information while providing users with useful information about contingencies arising from a business combination?

Yes. However, we believe the Board should reconsider these disclosure requirements. We believe the disclosures required under the proposed FSP related to acquired contingencies should not be greater than the disclosures related to contingencies arising in the normal course of business. We recommend that the Board determine what contingency disclosures should be required as a whole (ongoing business and acquired) in the SFAS 5 project that is currently underway and adjust FAS 141(R) disclosures to more closely align with current SFAS 5 disclosure requirements.