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Financial Accounting Standards Board 401 Merritt 7
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We appreciate the opportunity to respond to the Financial Accounting Standards Board's Exposure Draft for *Disclosure of Certain Loss Contingencies*, which would amend FASB Statements No. 5 and 141(R).

While we understand that directionally and appropriately, the Board's agenda is focused on international convergence with the resultant movement to International Financial Reporting Standards (IFRSs), this Exposure Draft (ED) would create divergence with the current and currently exposed IAS 37, *Provisions, Contingent Liabilities and Contingent Assets*. The FASB's ED notes that the disclosures in this proposed Statement are similar, but not identical, to those required by IAS 37. This proposed Statement would require disclosures about a broader population of contingencies than required by IAS 37.

Specifically, this proposed Statement would require disclosures about loss contingencies, regardless of the likelihood of loss, if the contingencies are expected to be resolved in the near term and if the contingencies could have a severe impact on the entity's financial position, cash flows, or results of operations. IAS 37 does not require disclosures for remote loss contingencies regardless of the expected timing of resolution or potential severity of the contingency. While the IASB is currently deliberating changes to IAS 37, it has not yet considered its disclosure requirements. The IASB's current ED, issued in 2005, is expected to be issued as a final standard in 2010. Accordingly, any changes for disclosure requirements will occur after that date.

This ED indicates that the FASB has issued this proposed statement as a result of investors and other users of financial information expressing concerns that disclosures about loss contingencies under the existing guidance in FAS 5, *Accounting for Contingencies*, do not provide adequate information to assist users of financial statements in assessing the likelihood, timing, and amount of future cash flows associated with loss contingencies.

However, disclosures concerning the types of loss contingencies outlined in the ED will not be sufficiently predictive in nature to improve the quality of information presented in the financial statements. We feel that due to the many uncertainties associated with loss contingencies, coupled with the wide range of volatility inherent in quantifications regarding such contingencies, disclosures required under the proposed ED could create misleading information and not be useful to readers of financial statements. We view the disclosures mandated in the ED, not as an improvement, but as a degradation of current reporting.

We respectively recommend that the FASB defer their ED for disclosure contingencies and converge any future requirements at such time that the IASB and/or FASB can harmonize requirements.

Furthermore, the largest area of concern regarding this ED is the impact on a company's litigation. Both unasserted and asserted claims are frequently brought for tactical or speculative purposes, when filed on behalf of plaintiffs' attorneys. Requiring premature valuation disclosure would greatly weaken a company's ability, to manage litigation risk to the prejudice of the company and its shareholders because opposing litigants would consider that information to set the "floor" for any settlement and because such disclosure would risk effecting a waiver of the privilege that otherwise would apply to litigation risk assessments.

Our comments to the questions raised in the ED are included below.

Request for Comments

1. Will the proposed Statement meet the project's objective of providing enhanced disclosures about loss contingencies so that the benefits of those disclosures justify the incremental costs? Why or why not? What costs do you expect to incur if the Board were to issue this proposed Statement in its current form as a final Statement? How could the Board further reduce the costs of applying these requirements without significantly reducing the benefits?

No, the proposed Statement will not meet the project's objective of providing enhanced disclosures about loss contingencies so that the benefits of those disclosures justify the incremental costs.

Disclosures concerning the types of loss contingencies outlined in the ED will not be sufficiently predictive in nature to improve the quality of information presented in the financial statements. We feel that due to the many uncertainties associated with loss contingencies, coupled with the wide range of volatility inherent in quantifications regarding such contingencies, disclosures required under the proposed ED could create misleading information and not be useful to readers of financial statements. We view the disclosures mandated in the ED, not as an improvement, but as a degradation of current reporting.

To require disclosure for a loss contingency involving an <u>unasserted</u> claim or assessment in which there has been <u>no manifestation</u> by a potential claimant where there could be the probability that a claim will be asserted and the likelihood of a loss, if the claim or assessment were to be asserted, is more than remote is <u>misleading</u> and inappropriate disclosure to the reader of the financial statements. The litigious overture that prevails today lends itself to many company significant claims, including those of a frivolous nature. Accordingly, many times it is difficult to judge whether there is any probability that unasserted lawsuits will be filed by plaintiffs' attorneys.

If estimates or ranges of estimates for unasserted claims are disclosed, the estimated ranges (either explicit or implicit) can be so large that these will be misleading and provide meaningless and inappropriate disclosures within the financial statements. Such disclosures will provide little or no value to users of these statements. The market could respond negatively to the disclosed numbers, even though they may not be accurate. Forcing a valuation of a case before there is sufficient information to make such a judgment is not helpful to the case or to the investing public.

Disclosures required under FAS 5 continue to be fit-for-purpose.

2. Do you agree with the Board's decision to include within the scope of this proposed Statement obligations that may result from withdrawal from a multiemployer plan for a portion of its unfunded benefit obligations, which are currently subject to provisions of Statement 5? Why or why not?

We believe the provisions outlined in Statement 5 are still appropriate.

3. Should an entity be required to provide disclosures about loss contingencies, regardless of the likelihood of loss, if the resolution of the contingencies is expected to occur within one year of the date of the financial statements and the loss contingencies could have a severe impact upon the operations of the entity? Why or why not?

The proposed disclosure requirement is counter-intuitive and misleading to users. For example, if a matter was potentially heading for trial within 12 months that could result in a judgment, which could have a severe impact upon the company's operations, a company would be required to disclose it, even if the company believes they would prevail. Furthermore, under the proposed disclosure requirements, a company will need to disclose how much is sought or estimate a loss in a case where it doesn't think it will lose anything.

Claims are frequently brought for tactical or speculative purposes on the part of the plaintiff. Requiring premature valuation disclosure would greatly weaken a company's ability to manage litigation risk to the prejudice of the company and its shareholders because opposing litigants would consider that information to set the "floor" for any settlement and because such disclosure would risk effecting a waiver of the privilege that otherwise would apply to litigation risk assessments.

In many cases, a company is only one of a group of defendants. Companies often don't know whether they have potential liability or the extent until well into discovery.

The extended nature and complexity of the legal process and the difficulty encountered in quantifying a claim with reasonable certainty – or applying a "more likely than not" filter, at least in the early stages exemplifies the many uncertainties of facts, duties, causation, loss, in addition to the uncertainty as to the law itself on given facts, that typically give rise to the more complex uncertainties arising in litigation.

With respect to similar cases that are aggregated, how would a company provide information about "the contingency, its current status, and the anticipated timing of its resolution?" It would be different for each matter.

Furthermore, no law firm will say that a matter is "remote" given current ABA advice and malpractice concerns. And, while clients often press attorneys for estimates of success in percentage terms, most commercial lawyers are often reluctant to provide them as they are seen as a misleading simplification that give claim positions a spurious reality.

Use of amounts that plaintiffs seek would result in grossly inflated numbers; however, conservative estimates of the exposure will likely yield unpleasant consequences if settlement is determined at high levels.

- 4. Paragraph 10 of Statement 5 requires entities to "give an estimate of the possible loss or range of loss or state that such an estimate cannot be made." One of the financial statement users' most significant concerns about disclosures under Statement 5's requirements is that the disclosures rarely include quantitative information. Rather, entities often state that the possible loss cannot be estimated. The Board decided to require entities to disclose the amount of the claim or assessment against the entity, or, if there is no claim of assessment amount, the entity's best estimate of the maximum possible exposure to loss. Additionally, entities would be permitted, but not required, to disclose the possible loss or range of loss if they believe the amount of the claim or assessment is not representative of the entity's actual exposure.
 - a. Do you believe that this change would result in an improvement in the reporting of quantitative information about loss contingencies? Why or why not?
 - b. Do you believe that disclosing the possible loss or range of loss should be required, rather than optional, if any entity believes the amount of the claim or assessment or its best estimate of the maximum possible exposure to loss is not representative of the entity's actual exposure? Why or why not?
 - c. If you disagree with the proposed requirements, what quantitative disclosures do you believe would best fulfill users' needs for quantitative information and at the same time not reveal significant information that may be prejudicial to an entity's position in a dispute?

We believe that disclosing estimates or ranges of estimates with no basis is not an improvement in the reporting process. Disclosures concerning the types of loss contingencies outlined in the ED will not be sufficiently predictive in nature to improve the quality of information presented in the financial statements. We feel that due to the many uncertainties associated with loss contingencies, coupled with the wide range of volatility inherent in quantifications regarding such contingencies, disclosures required under the proposed ED could create misleading information and not be useful to readers of financial statements. We view the disclosures mandated in the ED, not as an improvement, but as a degradation of current reporting.

See our response to questions 1 and 3 above.

5. If a loss contingency does not have a specific claim amount, will an entity be able to provide a reliable estimate of the maximum exposure to loss (as required by paragraph 7(a)) that is meaningful to users? Why or why not?

No, see our response to questions 1 and 3 above.

6. Financial statement users suggested that the Board require disclosure of settlement offers made between counterparties in a dispute. The Board decided not to require that disclosure because often those offers expire quickly and may not reflect the status of negotiations only a short time later. Should disclosure of the amount of settlement offers made by either party be required? Why or why not?

As noted by the Board, settlement offers expire quickly and may not reflect the status of negotiations at a subsequent time. Disclosure of settlement offers are exceedingly burdensome and would provide a roadmap to attorneys not involved in the applicable cases of a company's analysis of case value and negotiating strategy.

7. Will the tabular reconciliation of recognized loss contingencies, provided on an aggregated basis, provide useful information about loss contingencies for assessing future cash flows and understanding changes in the amounts recognized in the financial statements? Why or why not?

No, see our response to questions 1 and 3 above.

8. This proposed Statement includes a limited exemption from disclosing prejudicial information. Do you agree that such an exemption should be provided? Why or why not?

While we agree on the exemption from disclosing prejudicial information, we feel this exemption is somewhat limited due to the requirement of the fact the information may continue to be prejudicial when aggregated to a higher level, or if noted, that certain information <u>has not</u> been disclosed.

9. If you agree with providing a prejudicial exemption, do you agree with the two-step approach in paragraph 11? Why or why not? If not, what approach would you recommend and why?

See answer above. We recommend that the disclosure requirements outlined in FAS 5 continue to provide the framework for disclosing prejudicial information.

10. The International Accounting Standards Board (IASB) continues to deliberate changes to IAS 37, Provisions, Contingent Liabilities and Contingent Assets, but has not yet reconsidered the disclosure requirements. The existing disclosure requirements of IAS 37 include a prejudicial exemption with language indicating that the circumstances under which that exemption may be exercised are expected to be extremely rare. This proposed Statement includes language indicating that the circumstances under which the prejudicial exemption may be exercised are expected to be rare (instead of extremely rare). Do you agree with the Board's decision and, if so, why? If not, what do you recommend as an alternative and why?

We believe that the present disclosures under IAS 37 are consistent with FAS 5. IAS 37 defines a contingent liability as (a) a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or (b) a present obligation that arises from past events but is not recognized because (i) it is not possible that an outflow of resources embodying economic benefits will be required to settle the obligation; or (ii) the amount of the obligation cannot be measured with sufficient reliability. Accordingly, an entity, pursuant to IAS 37, should

not recognize a contingent liability. However, an entity should disclose a contingent liability, unless the possibility of an outflow of resources embodying economic benefits is remote.

The FASB's proposed ED, as outlined in our response to question 1 above, subjects companies to a higher and greater disclosure standard than IAS 37. Consistent with FAS 5, IAS 37 provides for meaningful disclosures of the nature of uncertainties, etc. without prejudice to disclosing estimates or ranges of estimates to outcomes.

11. Do you agree with the description of prejudicial information as information who "disclosure...could affect, to the entity's detriment, the outcome of the contingency itself"? If not, how would you describe or define prejudicial information and why?

We agree with the Board's general description of prejudicial information but continue to believe that the disclosure requirements outlined in FAS 5 are robust and appropriate.

12. Do you believe it is operational for entities to disclose all of the proposed requirements for interim and annual reporting periods? Should the tabular reconciliation be required only annually? Why or why not?

We do not believe that reporting tabular information proposed in the Board's ED is meaningful to users of financial statements inasmuch as it is not reflective of economic reality at that juncture.

We continue to believe that the disclosure requirements outlined in FAS 5 are fit-for-purpose and appropriate to users of financial statements.

13. Do you believe other information about loss contingencies should be disclosed that would not be required by this proposed Statement? If so, what other information would you require?

We continue to believe that the disclosure requirements outlined in FAS 5 are fit-for-purpose and appropriate to users of financial statements.

14. Do you believe it is operational for entities to implement the proposed Statement in fiscal years ending after December 15, 2008? Why or why not?

We do not believe it is operational for entities to implement the proposed Statement in fiscal years ending after December 15, 2008.

Sincerely,

Randy Braud Vice President

Controller US & Canada

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Shell Oil Company