



LETTER OF COMMENT NO. 40

File Reference No. 1600-100

Comments on Exposure Draft - Proposed Statement of Financial Accounting Standards, Disclosure of Certain Loss Contingencies, an amendment of FASB Statements No. 5 and 141(R).

Positive Impact of Exposure Draft:

- The exposure draft takes the proactive approach that all contingent losses must be disclosed, allowing specified exceptions, rather than the FASB 5 approach where you only have to disclose the liability if it reaches a certain probability threshold.
- The requirement for both financial and qualitative information about the nature of the risks will insure that stakeholders will be able to make better judgments than before as opposed to the current model of either accrual or disclosure.
- Finally the “Tabular Reconciliation” will spotlight each entity’s actual performance versus its estimated performance with regards to contingencies, giving incentives to management to be accurate.

Exposure Draft Falls Short:

According to the minutes of the March 9 2005 board meeting one of the reasons that the FASB was revisiting accounting for contingencies was because of problems with current standards on accounting for environmental liabilities. Environmental liabilities are somewhat unique in that they often manifest over long time periods, can be very large, subject to legislative change, and subject to evolving knowledge and science. There are other types of liabilities such as product safety or medical types of liabilities which also fall into these categories. For the sake of simplicity, I will call these liabilities in the early stage of evolution since so much is unknown about their final resolution. For such liabilities in particular, I believe that the exposure draft falls short in two areas.

- In the March 9, 2005 board meeting the FASB agreed that when many similar remote liabilities existed that they should be aggregated in the determining of probabilities. However, The Rose Foundation stated that this was not the case in current practice. The concept of having **many single remote liabilities equal one possible or probable liability** is addressed in one section of the exposure draft not in another where it is critical for accurate disclosure.
 - **Addressed: in paragraph 6** of the exposure draft when discussing liabilities that must be disclosed (if they are to be resolved in the next year with disruptive effect on the firm) it is stated that a “loss contingency, or a combination of loss contingencies” will be evaluated.
 - **Not addressed: in paragraph 5** when determining if an unclaimed liability is “remote” or “probable” for inclusion, the wording is simply all loss contingencies.

I believe that if paragraph 5 is not changed to wording such as “ an entity shall disclose all loss contingencies or combination of loss contingencies....” a large number of early evolution type liabilities that will eventually have detrimental financial impact on the entity will fail to be disclosed in the financial statements.

- Paragraph 6 defines contingencies which must be disclosed under any circumstances. These contingencies are those that “regardless of the likelihood of the loss” will be resolved within the next year and would “disrupt the normal functioning of the entity”. It is my contention that there are many early stage contingencies that could potentially “disrupt the normal functioning of an entity” that financial statement users would be interested in. Many of these contingencies will not be resolved for many years. Therefore I believe that requiring both resolution within one year and disruption of the normal functioning of the entity is overly restrictive. I believe that either condition should be sufficient for disclosure.

Thank you for considering these comments.

Sincerely,

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