

# McGladrey & Pullen

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March 31, 2009

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



LETTER OF COMMENT NO. 264

## File Reference: Proposed FSP FAS 157-e

Dear Mr. Golden:

We are pleased to comment on the proposed FASB Staff Position (FSP) No. FAS 157-e, *Determining Whether a Market Is Not Active and a Transaction Is Not Distressed*. We support the efforts of the FASB to provide additional guidance on determining whether a market for a financial asset is not active and a transaction is not distressed and to determine the fair values of such financial assets when the only quoted prices for similar assets are associated with inactive markets or distressed sales.

We have the following three primary concerns with respect to the proposed staff position:

1. We believe that in order to presume that a quoted price is associated with a distressed transaction, management should be required to undertake reasonable efforts to determine whether the factors set forth in Step 2 are present for a given quoted price. As drafted ("unless the reporting entity has evidence that indicates that both of the following factors are present for a given price"), we believe management may conclude that they are not required to make any effort to determine whether such evidence exists, which is contrary to the requirement in the preceding sentence to "evaluate the quoted price to determine whether the quoted price is associated with a distressed transaction." We suggest that the final FSP impose upon management a specific requirement to undertake reasonable efforts to determine whether such evidence exists and that the phrases "the reporting entity has/does not have evidence" be replaced with "the reporting entity is unable to obtain". Language similar to that found in paragraph 30 of Statement of Financial Accounting Standards No. 157, *Fair Value Measurement* (FAS 157), could be used to describe the level of effort required.
2. The final paragraph of Paragraph 29A is unclear as to whether a quoted price associated with a distressed transaction should be considered (but adjusted) in determining the fair value of a similar financial asset or whether that information is deemed to be irrelevant and should not be considered. We believe that in order for preparers and auditors to consistently apply the guidance in the proposed FSP, this must be clarified.
3. We believe the example set forth in paragraphs A32A through A32G may encourage management to simply "split the difference" as opposed to making its best estimate of fair value based on an exit price notion using an appropriate Level 3 model. If this example is retained, we believe the example should articulate why the midpoint represents the best estimate of fair value in the circumstances.

## Comments on Specific Issues Requested by the FASB

*Issue 1: Is the proposed effective date of interim and annual periods ending after March 15, 2009, operational?*

We believe the proposed effective date will be operational for some, but not all entities and suggest an effective date of interim and annual periods ending after June 15, 2009 with earlier application permitted for interim and annual periods ending after March 15, 2009.

*Issue 2: Will this proposed FSP meet the project's objective to improve financial reporting by addressing fair value measurement application issues identified by constituents related to determining whether a market is not active and a transaction is not distressed? Do you believe the amendments to Statement 157 in this proposed FSP are necessary, or do you believe the current requirements in Statement 157 should be retained?*

The discussion in paragraph 15 and the example in paragraphs A32A through A32G of the proposed FSP raise questions about whether the results of the valuation technique are intended to result in a fair value measurement consistent with FAS 157. The terminology used is not consistent with the terminology of FAS 157, and the key principles of FAS 157 are not discussed or referenced. The discussion in paragraph 9a of FSP FAS 157-3, *Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active*, articulated the key existing principles when that FSP was issued. We believe this proposed FSP should contain similar linkage to FAS 157.

*Issue 3: Do you believe the proposed two-step model for determining whether a market is not active and a transaction is not distressed is understandable and operational? If not, please suggest alternative ways of identifying inactive markets and distressed transactions.*

Subject to our preceding comments, we believe the two-step model proposed is understandable and operational. However, we are concerned that if quoted prices for distressed transactions for similar transactions should be considered but adjusted, the proposed FSP does not provide any guidance about how to adjust that quoted price. The lack of any guidance about how to adjust such prices will potentially lead to minimal use of observable data when determining fair value in a market that is not active. This direction is inconsistent with a stated objective about valuation inputs in paragraph 7 of FAS 157: "Valuation techniques used to measure fair value shall maximize the use of observable inputs and minimize the use of unobservable inputs." At a minimum, we suggest the proposed FSP be revised to:

- Provide guidance on what factors should be considered in making adjustments to quotes associated with distressed transactions
- Make it an explicit presumption that prices observed in distressed transactions be considered and adjusted to reflect the amounts that management concludes would have resulted from in a non-distressed transaction between a willing buyer and a willing seller

*Issue 4: Are the factors listed in paragraph 11 of the FSP that indicate that a market is not active appropriate? Please provide any other factors that indicate that a market is not active.*

We believe the factors identified are appropriate and will be helpful to preparers and auditors.

*Issue 5: What costs do you expect to 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 of the FSP without reducing the benefits?*

We believe the costs to implement the proposed FSP could be significant, however we are unable to determine at this time.

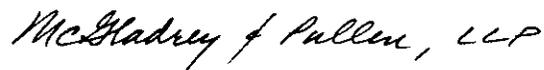
## Other Comments

We offer the following additional comments:

- We suggest "(significant judgment is required)" be deleted at the end of the first paragraph in new paragraph 29A because that point is made in the concluding paragraph of Step 1 and this may imply a higher degree of latitude in determining whether a market is not active than the Board intended.
- In Step 1, subparagraph e of new paragraph 29A refers to "credit and other nonperformance risk for the asset class". We believe the word "class" should be deleted as it is not consistent with prior language and may be applied too broadly (e.g., to all collateralized debt obligations rather than to similar tranches of similar securities).
- In Step 2 subparagraph a, the reference is to the period before the "measurement date". We believe this should more appropriately refer to the "transaction date".
- The sentence in the last paragraph under Step 2 states "However, the fair value resulting from the present value technique shall not be derived solely from inputs based on the quoted price associated with a distressed transaction." This should be revised to better balance it with the idea that while prices in transactions deemed to be distressed under this proposed FSP require significant adjustment, they still provide relevant information useful in measuring fair value.
- We suggest eliminating the phrase "for bearing uncertainty" from the last sentence in the past paragraph under Step 2 since all factors in the measure of fair value relate to uncertainties.
- In paragraph A 32B, we suggest "similarly rated" be inserted before "collateralized debt obligations."

We would be pleased to respond to any questions the Board or its staff may have about any of the preceding comments. Please direct any questions to either Jay D. Hanson (952-921-7785) or Jolene M. Hart (952-921-7735).

Sincerely,



McGladrey & Pullen, LLP