



Via Email

July 10, 2009

Mr. Robert Herz  
Chairman  
Financial Accounting Standards Board  
P.O. Box 5116  
Norwalk, Connecticut 06856-5116

Sir David Tweedie  
Chairman  
International Accounting Standards Board  
30 Cannon Street  
London, EC4M 6XH  
United Kingdom

Re: Project on Financial Instruments – Improvements to Recognition and Measurement

Dear Chairman Herz and Chairman Tweedie:

In conjunction with the Financial Accounting Standards Board's ("FASB") and International Accounting Standards Board's ("IASB") (collectively, the "Boards") aforementioned joint project, the Investors Technical Advisory Committee ("ITAC") would like to take this opportunity to share its principal views on the accounting for financial instruments for your consideration during the development and formulation stage. Our input is based upon our perceptions as users of financial statements and our goal is to improve the clarity, completeness, and usefulness of financial reports.<sup>1</sup>

ITAC supports the FASB and IASB on the overarching goal of their joint financial instruments accounting project "to significantly improve the decision usefulness of financial instrument reporting for users of financial statements." ITAC previously provided its comments on the Boards' March 28, 2008 Invitation to Comment, *Reducing*

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<sup>1</sup> This letter represents the views of the Investors Technical Advisory Committee ("ITAC") and does not necessarily represent the views of its individual members or the organizations by which they are employed. ITAC views are developed by the members of ITAC independent of the views of the Financial Accounting Standards Board ("FASB") and its staff. For more information about the ITAC, including a listing of the current members and the organizations in which they are employed, see [http://www.fasb.org/investors\\_technical\\_advisory\\_committee/itac\\_members.shtml](http://www.fasb.org/investors_technical_advisory_committee/itac_members.shtml).

*Complexity in Reporting Financial Instruments.*<sup>2</sup> As the FASB and IASB formulate their exposure drafts on the classification and measurement phase of the project we would like to reiterate our previously expressed views.

Given that financial statement users have expressed significant concern over the current mixed-attribute accounting model for financial instruments – concerns which were exacerbated by the unfortunate experiences of the recent past – we are pleased that both Boards are tackling these urgent and complex issues. That said, we would like to urge the Boards to strive to work together on their respective projects and attempt to come to converged conclusions that can be viewed by all stakeholders as an undisputed high quality international standard. We are troubled by the apparent lack of coordination on the progression and development of concepts between the two standard setters as it relates to these projects as we fear that the Boards could create additional differences between their respective standards given their current paths. The FASB’s and IASB’s actions could result in different accounting models, which would not only allow accounting arbitrage within a set of standards, but between U.S. generally accepted accounting principles and international financial reporting standards. If the two Boards issue standards that contain different models after a stated goal of convergence, we believe this could lead to an unfortunate environment where the accounting standard setting process becomes further politicized.

To be clear, the ITAC will not support a converged standard in connection with this project, or any FASB or IASB project, if the converged standard does not, in our view, improve the clarity, completeness, and usefulness of financial reports. We strongly urge the FASB and IASB to work together to produce a single, high-quality standard that meets the needs of financial statement users.

In our comment letter of September 17, 2008, we stated our opinion that fair value is the only measurement method for financial instruments that meets the needs of investors.<sup>3</sup> More specifically, we stated:

We believe that investors would benefit greatly, and financial reporting in general would be substantially improved, if a single and consistent measurement-basis were to be used for all financial instruments. We also concur with the Boards’ view that this measurement method should be fair value and **believe the Boards should require fair value as the only measurement method for financial instruments.** We hold this view for several reasons.

First, and most importantly, fair value measures reflect the most current, complete and accurate estimates of the value of financial instruments, and

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<sup>2</sup> Letter from Michael Moran, Member, ITAC, to Mr. Robert Herz, Chairman, FASB and Sir David Tweedie, Chairman, International Accounting Standards Board (“IASB”) (Sept. 17, 2008), <http://www.iasb.org/NR/rdonlyres/A76C7FF2-E5F0-4585-8322-E7C44539E025/0/CL29.pdf>

<sup>3</sup> See Letter from Michael Moran at 1.

are based upon an up-to-date assessment of the amounts, timing, and riskiness of the future cash flows attributable to the asset or obligation. As market conditions change, the values, risk profiles and prospective cash flows of financial instruments change as well. It is essential that investors, who provide capital to companies and bear risk as a result, have a clear understanding of the effects of these changes.<sup>4</sup>

Further, our September 17, 2008 letter expressed our belief that changes in fair value should be clearly and visibly presented on the face of financial statements and sufficiently disaggregated by line item; fair value changes should not be buried and obscured in a reconciliation of accumulated other comprehensive income outside of the earnings statement.

We noted that “the current global financial crisis ... has highlighted the widespread exposure to financial instruments and the need for timely, relevant information on the value of such securities and risks.”<sup>5</sup> In addition, our letter pointed out that mixed-attribute models “obscure the effects of a company’s financial arrangements on its operations and make financial statement analysis a daunting task, even for the highly experienced and savvy financial statement user,” and that the “current mixed-attribute model ... creates structuring opportunities to achieve a particular accounting effect.”<sup>6</sup>

An often heard critique of fair value accounting is that it is pro-cyclical and introduces unnecessary volatility to the capital markets. Such criticism will always be anchored on subjective opinions that are not under the purview of standard accounting practice. It is not the role of accountants to make directional bets on the capital markets. Or more simply put: who is to say that the disruptions we see at one time will not be followed by greater turmoil and further reductions in the fair value of financial assets? Accounting is meant to give an *objective* view of the financial condition of the reporting entity at a given point in time. Articulating a *subjective* interpretation of an accounting report is the responsibility of regulators, investors, credit officers, counter parties and other participants in the capital markets. The FASB and IASB should never tire of reminding market participants, and others, of this.

An important component of any standard is the accompanying disclosures. Thus, we believe that, *as part of the current project*, the Boards should require additional disclosures in the notes to the financial statements. The disclosures should be transparent and insightful, and sufficient to enable investors to adequately evaluate the potential risks and rewards associated with financial assets and liabilities and their use as part a company’s operating, investing and financing activities, including the current and potential effects of the instruments on cash-flow and liquidity.

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<sup>4</sup> *Id.* at 1-2.

<sup>5</sup> *Id.* at 2.

<sup>6</sup> *Id.*

To usefully complete and more comprehensively address the all-important fair value measurement aspect of the financial instruments standard, please see our proposal for a “principles-based” disclosure standard<sup>7</sup> in the letter that ITAC submitted to the FASB on December 11, 2008 (a copy of which was sent to the IASB). It is our understanding that Chairman Herz has decided to add such a project to the FASB’s agenda, and we strongly support the FASB on this endeavor.

We also understand that our framework proposal was shared with the IASB and its staff in conjunction with ITAC’s participation in the IASB’s Standards Advisory Committee and the Analyst Representative Group. In our letter we suggested three primary disclosure areas:

- **“General”** – outlining the basis of presentation for that particular account/financial statement line item (e.g., in a manner similar to information presented currently under “significant accounting policies” – this will serve to replace or substitute the information currently presented in that caption);
- **“Composition”** – outlining what is included in the account/line item (e.g., item breakdown and netting – such as loans net of provisions) and also providing a roll-forward when appropriate (including amounts attributed to increases or decreases arising from changes in estimates), and
- **“Assumptions and Uncertainties”** – outlining principal assumptions, estimates, sensitivity analyses, and a qualitative discussion regarding risks and uncertainties and the potential of the amounts to change over time.<sup>8</sup>

Although these areas were proposed as necessary components of a general disclosure framework, we believe these concepts could be applied to financial assets and liabilities and would serve to meaningfully enhance users’ understanding of the potential effects of financial instruments on a company’s future operating, investing, and financing activities. Consequently, we would suggest that the FASB and IASB consider them, and the overall concept of a disclosure framework, as part of this project. In addition, we would strongly encourage the FASB and IASB to consider a similar fair value disclosure framework for those instruments or exposures that are not recorded on a company’s balance sheet, including their fair value and effects on earnings. Such information should provide sufficient information to enable investors to evaluate the potential effects of off balance sheet activities and exposure on the company’s future operating, investing, and financing activities.

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<sup>7</sup> Letter from Mike Gyure, Member, ITAC, to Mr. Robert Herz, Chairman, FASB and Sir David Tweedie, Chairman, IASB (Dec. 11, 2007), <http://www.fasb.org/jsp/FASB/Page/ITACDisclosureProposal.pdf>

<sup>8</sup> Letter from Mike Gyure at 2-3.

We appreciate the opportunity to share our views on the classification and measurement phase of your project on accounting for financial instruments. Should the Boards or your staff have questions about our views or wish to discuss over views further, please contact the undersigned or any member of the ITAC.

Sincerely,

Investors Technical Advisory Committee

By:

/s/ Janet L. Pegg

Janet L. Pegg  
Member, ITAC

CC: Kevin Stoklosa, Assistant Director, FASB  
Sue Lloyd, Senior Technical Consultant, IASB