From: M. A. Gumport [mailto:magumport@att.net] Sent: Wednesday, September 23, 2009 8:08 PM

To: Robert Herz

Subject: Yes, you have heard this from me before: It's time to tack. The FASB's opportunity is

here and now...

Bob:

You may recall I worked as an institutionally recognized securities analyst for over twenty years and then served as director and/or CFO of several venture technology companies, two of which went public. I now head a corporate finance advisory startup.

I just read the minutes reporting the FASB's 8/27/09 meeting on "Financial Instruments with Characteristics of Equity". The discussion pertained to the circumstances determining whether certain instruments would be classified as liabilities or equity.

The 8/27/09 minutes seem to reflect some uncertainty among the meeting's participants as to the appropriateness of shaving distinctions finer and finer in seeking to dispatch instruments as "equity" or "liabilities". I hope the FASB found the session good practice, because, as soon as the currently proposed rules governing the accounting treatment of liabilities and equity are finalized, the FASB almost certainly will be up to its eyeballs dealing with variations on a similar theme: In years to come, a barrage of "innovations" will be launched to "game the system", and the parties will descend upon the FASB for corroboration.

After over 20 years of work on the equity/liability project, the FASB stands at a fork in the road.

Down the first path, the FASB proposes to perpetuate existing convention that accords differential treatment to "debt" and "equity" liabilities. The new rules refine but perpetuate the current ones governing the accounting treatment of "debt" versus "equity". Today's equity accounting rules, and the proposed new ones, exempt a firm's equity instruments from being marked to market or, in any case, permit any change in value of equity instruments to bypass the income statement.

Down the second path, the FASB could choose to have accounting treat "debt" and "equity" similarly, and there the debate ends. Accounting's clarity and efficiency would be improved and the FASB set free to address other, substantive issues.

If the FASB maintains its current course, it will stumble directly into years more of tedious, definitional argumentation of which the 8/27/09 experience was the tamest exemplar. A cavalcade of interests will soon launch arguments as to why some set of features and circumstances demands in part to be treated as equity, in part as debt, and each new FASB ruling will invite an onslaught of counterattacks. The FASB will be reduced to a game of "whack a mole".

Why not take the other road at this crucial juncture? The distinctions between "debt" and "equity" are real, but the accounting distinction between the treatment of "debt" and "equity" is entirely artificial. In its treatment of equity, "modern" accounting harks back to before the first issuance of public equity securities in the early 17th century. With the value of public equity in the 21st century readily recognized and monetized, isn't it time to truly modernize accounting and treat equity like any other asset or liability?

From the standpoint of accounting clarity and reporting simplicity, abolishment of the distinction between the treatment of debt liabilities and equity liabilities would be a great accomplishment: Let both be marked to market with gains/losses recognized in the income statement.

Unless the FASB changes course, then the 8/27/09 FASB meeting is just a taste of what is to come: Endless, inconclusive debate on a procession of instruments and circumstances that demand consideration as "debt", "equity" or in part one, in part the other. The FASB's deliberations on these refinements, however well intentioned, inevitably will appear capricious as distinctions become ever more refined. Though such a an outcome may be good guarantee full employement for accountants (and substantially help attorneys and bankers, too), I cannot imagine that is the legacy you wish to leave behind. It's time to tack. The opportunity is here and now. End the distinctive treatment of equity liabilities; put equity on an even footing with other liabilities.

Regards,

Mike

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