1840-100 Comment Letter No. 158

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BY EMAIL: director@fasb.org

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

Re: File Reference No. 1840-100

Dear Mr. Golden:

We appreciate the opportunity to comment on the July 20, 2010 Proposed Accounting Standards Update on Disclosure of Certain Loss Contingencies (the "Proposed Update"). Dewey & LeBoeuf LLP is an international law firm headquartered in New York with more than 1,200 lawyers in 15 countries. We represent clients in virtually every major industry sector, including many major domestic and international insurance companies.

Our firm submitted two comment letters on the FASB's Exposure Draft, Disclosure of Certain Loss Contingencies, dated June 5, 2008 (the "2008 Exposure Draft"), and one of our partners, Richard W. Reinthaler, participated in the FASB's March 2008 roundtable discussion on the 2008 Exposure Draft.

We applaud the FASB's attempt to address many of the concerns we (and others) expressed in prior comment letters regarding the 2008 Exposure Draft and during the FASB roundtable discussion. While the Proposed Update represents a significant improvement from the 2008 Exposure Draft, it unfortunately does not adequately address or alleviate all of the concerns previously expressed. In fact, it raises a number of new concerns, discussed below, that, in our view, if adopted, would:

- give an unfair advantage to the plaintiffs' bar by requiring disclosure of certain types of prejudicial information (e.g., average settlement amounts, individual accruals for litigation loss contingencies in financial statement footnotes, and the coverage positions of insurers even if not discoverable under applicable law);
- increase the risk of disputes with auditors over the level of disclosure required from outside counsel and, potentially, the erosion of the attorney-client privilege and work product doctrine that additional auditor due diligence will entail;
- impose new standards of disclosure and aggregation, with inadequate guidance or explanation of the standard entities should employ; and
- impose substantial, and perhaps insurmountable, practical problems for public companies in implementing the new standard on the proposed timetable.

In discussions with our major public company clients, including insurance companies, we have identified four critical issues with respect to the Proposed Update that are of particular concern.¹ The focus of this letter will be limited to these critical concerns.²

We note that the Proposed Update makes clear that its scope is limited with respect to insurance companies and is not intended to apply to the accounting for insurance contracts and policies, which is covered by ASC Topic 944.

We have other significant concerns with respect to the Proposed Update that are not addressed in this letter that have been addressed by other commentators. These include:

[•] The requirement that an entity in assessing the materiality of a loss contingency may not consider possible insurance recoveries (which in our view makes little sense given that the net result will be the disclosure of extensive new information regarding immaterial loss contingencies);

[•] The requirement that disclosure must be made about certain "remote" loss contingencies that may have a potential "severe impact" (which in our view will likely result in less, rather than more, disclosure and confuse and mislead financial statement users who may have difficulty understanding the significant distinction in terms of risk exposure between "remote" and non-remote contingencies); and

[•] The deletion of the initially proposed "prejudicial" exemption from disclosure. We join in these objections.

I. THE PROPOSED EFFECTIVE DATE FOR PUBLIC COMPANIES IS UNWORKABLE AND SHOULD BE REVISED.

The Proposed Update contemplates that the new standard would be effective for fiscal years *ending* after December 15, 2010, and interim and annual periods in subsequent fiscal years, except for non-public entities, for which the standard would be effective for the first annual period beginning after December 15, 2010, and for interim periods of fiscal years after the first annual period. *Proposed Update at 450-20-65-1*.

Many of our major clients are public companies with fiscal years ending December 31. Requiring public companies to apply the new standard to their 2010 yearend financial statements is unworkable. Every one of our clients with whom we have spoken has told us that implementing the new standard beginning December 15, 2010 will create an administrative nightmare for them and is completely impractical. Given the complexity of some of the new concepts included in the Proposed Update, public companies will need more than three months to prepare for the application of the new standard, which may be further modified following receipt and consideration of comments to the Proposed Update. As but one example, we are advised that it will take a significant amount of time and effort for public companies, including in particular insurance companies which are heavily regulated by the states and are required to prepare financial statements that are in accordance with statutory accounting principles (as well as GAAP financials), to develop systems to (i) analyze and gather all of the additional quantitative and qualitative information for individual loss contingencies to be disclosed under the Proposed Update; (ii) provide the necessary level of detail required to determine the appropriate classification system for aggregating disclosures about loss contingencies; and (iii) classify loss contingencies for the required tabular reconciliation, which will be similar but not necessarily identical to the classification system for aggregating disclosures about loss contingencies.

In short, we believe that the proposed effective date for public companies is impractical and should be delayed. The proposed effective date for non-public entities presents a much more reasonable approach and we suggest that the same effective date be applied to public companies.

II. A TABULAR RECONCILIATION BY CLASS OF CONTINGENCIES WILL RESULT IN DISCLOSURE OF PREJUDICIAL INFORMATION.

The Proposed Update would not only require public companies for the first time to report in footnote disclosure the amounts accrued for individual loss contingencies. It would require entities to include in financial statements a reconciliation by class, in tabular format, of recognized (accrued) loss contingencies, which would include (i) carrying amounts of the accruals at the beginning and end of the period, (ii)

the amount accrued during the period for new loss contingencies, (iii) increases for changes in estimates for loss contingencies recognized in prior periods, (iv) decreases for changes in estimates for loss contingencies recognized in prior periods, and (v) decreases for cash payments or other forms of settlements during the period. *Proposed Update at* 450-20-50-1F(g).

Requiring disclosure of individual accruals and a tabular reconciliation (by class) of changes in accruals will in our view likely result in the disclosure of highly prejudicial information (i.e., an entity's personal assessment of the amount or range of loss), because the requirement that tabular reconciliations be prepared by class will as a practical matter for many public companies amount to disclosure of accruals on an individual litigation basis. For example, a public holding company may face at any one time (i) a material class action securities lawsuit; (ii) a material consumer fraud class action challenging the company's sales practices; (iii) a material age or sex discrimination class action lawsuit; (iv) a large lender liability case; (v) significant environmental/real estate litigation; (vi) intellectual property litigation that challenges a critical product; and (vii) derivatives litigation of one type or another emanating from the company's efforts to hedge its investment risks. Each of these individual material contingencies, as we read the Proposed Update, may have to be included in a separate tabular reconciliation as none of them would appear to fall within the same "class." Once individual accruals are disclosed (or can be traced through changes in tabular reconciliations), one thing is virtually certain: the plaintiffs' bar will seek discovery regarding the basis for these public disclosures/accruals. This is particularly troubling given that, unlike the 2008 Exposure Draft, the Proposed Update no longer contains an exemption from the new disclosure requirements for "prejudicial" information. Because many litigation accruals reflect settlement offers that have been made, requiring disclosure of individual accruals may also have the unintended effect of requiring disclosure of settlement offers, which is something the Proposed Update agrees would be prejudicial and thus need not be disclosed.

In short, we believe that the only disclosure of accruals that makes sense is one that would require disclosure of all material litigation loss contingencies in a single, aggregated reconciliation (as opposed to "by class"), which will allow financial statement users to track changes in accruals without jeopardizing the entity's overall risk exposure or settlement strategy.

III. IMPLEMENTATION GUIDANCE DISCOURAGES AGGREGATION OF LOSS CONTINGENCIES.

Under the Proposed Update, if a company provides disclosure on an aggregated basis, it must disclose sufficient information to enable financial statement users to understand the nature, potential magnitude and potential timing of the

contingency. Aggregation makes a great deal of sense when an entity faces a large number of similar claims, each of which may be immaterial but which in the aggregate could have a material impact on a reporting company's financial statements. Aggregation also makes sense where an entity faces a smaller number of similar (if not entirely duplicative) claims, such as multiple class actions alleging the same claims in different jurisdictions that have not yet been consolidated (or may not be subject to consolidation). Aggregation should be encouraged, not discouraged, in such situations.

The Proposed Update, however, rather than encouraging aggregated disclosure in such cases, actually *discourages* aggregated disclosure by

- suggesting that aggregated disclosure be limited in certain circumstances "by state" (if, for example, the states in question have differing speeds of disposition of cases, more plaintiff-friendly judicial systems, different statutes of limitation or other legal defenses to claims, etc.) (*Proposed Update at 450-20-55-1A*); and
- requiring disclosure of "average settlement amounts" (which in many instances is a meaningless statistic or a distorted number influenced by one or more aberrational outcomes that may not by indicative of future settlements) (*Proposed Update at 450-20-55-1D*). Moreover, disclosure of "average settlement amounts" will give plaintiffs a bargaining chip they currently may not have, as they will undoubtedly use the "average settlement amount" as a new "floor" in settlement negotiations, thereby increasing the risk that reporting companies (and their insurers) will end up paying more to settle future cases. Settlement amounts are also typically confidential and not discoverable by plaintiffs in other cases; the required disclosure would thus provide the plaintiffs' bar with information that is not currently publicly available, the disclosure of which would be highly prejudicial.

Accordingly, we urge the FASB to revise its proposal to delete any implementation guidance suggesting that average settlement amounts be disclosed or otherwise discouraging public companies from reporting loss contingencies, as appropriate, on an aggregated basis.

IV. DISCLOSURE ABOUT POSSIBLE INSURANCE RECOVERIES AND COVERAGE POSITIONS WILL RESULT IN DISCLOSURE OF PREJUDICIAL INFORMATION.

Finally, we note that the Proposed Update would require disclosure of information about possible recoveries from insurance and other sources, but only if and to

the extent that it has been provided to the plaintiff or is discoverable. Proposed Update at 450-20-50-1F(e)(5). A company would be required to determine if information about possible insurance recoveries is discoverable by the plaintiff and, if that information is discoverable, the company would be required to disclose the information in its financial statements even if the plaintiff has not requested that information or otherwise sought its discovery. This is troubling for several reasons:

Even if the plaintiff did seek discovery of this information, its disclosure in Federal court and many other legal jurisdictions would almost always be covered by a protective order, because courts understand that the disclosure of insurance coverage could easily spark new litigation. Yet, under the Proposed Update, this very information would be required to be publicly released *without* any confidentiality protections. Similar concerns arise in connection with any requirement to disclose average settlement amounts. This disclosure would materially affect current practices of the litigation process and skew its inherent fairness.

The Proposed Update goes even further, by requiring disclosure of the coverage position of any insurer with respect to each individual loss contingency, whether or not such information is known to the plaintiff or discoverable. If adopted, this will likely lead to the disclosure of prejudicial (and in many cases meaningless) information. Insurance companies frequently "reserve" their positions on coverage (on every conceivable, colorable basis) whenever material litigation is commenced. Disclosing the existence or receipt of a "reservation of rights" letter would not appear to be useful, may very well cause confusion, and thus would be unhelpful to the user of financial statements. Disclosing a coverage position that is contested, and the conflicting positions of the insured and insurer, may also impede resolution of their differences and provide fodder for discovery by the plaintiffs' bar. This is particularly troubling given that, unlike the 2008 Exposure Draft, the Proposed Update no longer contains an exemption from the disclosure of prejudicial information.

We urge the FASB to revise its proposal to limit the requirement to disclose information about possible insurance recoveries to information that has been provided to the plaintiff. The requirement to disclose information about possible insurance recoveries that is discoverable, as well as the requirement that information about the insurance coverage positions taken be disclosed in all instances, should be removed.

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If you have any questions regarding this letter, please feel free to contact Richard W. Reinthaler (212-259-6090; rreinthaler@dl.com); K. Oliver Rust (212-259-8571; krust@dl.com); John M. Schwolsky (212-259-8667; jschwolsky@dl.com); or Joseph L. Seiler III (212-259-8137; jseiler@dl.com) in our New York office.

Very truly yours,

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