

PAUL BARNES
Managing Director
Global Leader - Valuation Advisory Services
TEL 215.430.6025
paul.barnes@duffandphelps.com

DUFF & PHELPS

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Technical Director
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

File Reference: No. 1710-100

Duff & Phelps Corporation (NYSE: DUF) appreciates the opportunity to provide comments on the Exposure Draft of a proposed Accounting Standards Update related to Topic 820 – Fair Value Measurements and Disclosures.

We would be pleased to further discuss our comments with the Board and staff. Please direct any questions to Paul Barnes at (215) 430-6025 or David Larsen at (415) 693-5330.

Sincerely,

/s/ Paul F. Barnes

/s/ David L. Larsen

Paul F. Barnes
Managing Director

David L. Larsen, CPA
Managing Director

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Responses to Specific Questions:

Issue 1: With respect to the disclosure of the effect of changes in reasonably possible, significant, alternative inputs for Level 3 fair value measurements for each class of assets and liabilities (sometimes also referred to as sensitivity disclosures), the Board is seeking input from:

1. Financial statement preparers about their operationality and costs
2. IFRS financial statement preparers about the approach they plan to use to comply with a similar disclosure requirement in IFRS 7
3. Financial statements users about their usefulness—more specifically, a discussion of how they would benefit from, and use, such disclosures.

Duff and Phelps Response to Issue 1, Question 1:

We believe that in the context of determining a fair value estimate using Level 3 inputs, the notions of *reasonably possible* and *significant* are sufficiently open to interpretation and can result in substantial divergence in the implementation of the proposed ASU.

We understand that the Board is aiming to provide users with information on the sensitivity of fair value measurements to changes in the main valuation inputs. However, we believe that basing the sensitivity on *reasonably possible* alternative assumptions that would change fair value significantly, as proposed, is too broad. We understand that *reasonably possible* is defined by the ASC Master Glossary as:

“The chance of the future event or events occurring is more than remote but less than likely.”

An interpretation of the guidance above for an input with a normal distribution (as an example), would be that the input values anywhere between the 10th to the 80th percentiles could all be considered *reasonably possible* alternative assumptions. In many cases, the use of these inputs could result in significant changes in the fair values. We believe that providing a sensitivity analysis based on such a wide range of inputs may have the following unintended effects:

- Produce information that is too broad and overly complex, so its usefulness would be compromised;
- Highlight overly pessimistic or overly optimistic potential outcomes by considering the near-extreme point of the range of all possible inputs, neither of which is likely to occur, and therefore being of debatable informational value;
- In hindsight, this broad disclosure may lead to the second-guessing of judgments made that were appropriate at the valuation date. What was known or knowable as of the valuation date could be challenged. Could this lead to restatements where a current or a prospective fair value adjustment may be called for instead? It may also lead to increased risk of litigation

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challenging past judgments made in good faith, especially considering that judgments are inherently subjective.

- Lead to increased costs of compliance, at times by a considerable amount; meanwhile, fair value measurements in Level 3 are to be based on assumptions that are reasonably available *without undue cost and effort* (ASC Topic 820).

Comments on Recurring Fair Value Measurements (Specifically, Alternative Investments)

Based on our discussions with preparers and our work with clients who value financial instruments using Level 3 inputs, we do not believe the proposed ASU is operational and we expect that considerable additional cost and effort will be required to comply with the proposal.

Some preparers, including private equity buy-out managers, use multiple techniques and multiple inputs in estimating fair value. These techniques and inputs are used to triangulate around management's best estimate of fair value. Even if the proposal is interpreted as requiring disclosure of the end points of a "reasonable" range around the point estimate, the proposal is unclear on how such ranges would be aggregated and disclosed for each asset or liability class. Should the ranges be weighted based on the size of each underlying investment or should the range be the simple sum of the end points? Because of the portfolio effect of multiple investments in a class, an aggregate range determined by simply adding the individual ranges of individual investments could result in an overall range which itself would not be reasonable. While it may be reasonably possible that each individual investment could be valued using inputs resulting in certain ranges of value, it is much less likely that it is reasonably possible that all investments would be valued using the low end of their respective ranges or that all investments would be valued using the high end of their respective ranges. For this reason, we do not believe that this proposed disclosure will provide decision useful information. In addition, we believe that the incremental cost of compliance with the proposed guidance may be prohibitive for some reporting entities. We have provided a more detailed discussion of this issue in the Additional Comments section of this letter.

Other preparers, including venture capital managers and mezzanine debt managers, may use only one technique with one set of inputs to estimate fair value. Because the proposal asks for reasonably possible alternatives to be evaluated, the proposal may be interpreted as requiring management of such firms to use techniques that they did not deem necessary in coming to the point estimate of fair value. If this is the case, such reporters would be required to create new processes and procedures to identify possible other alternative techniques and inputs. In addition to the opportunity cost of management time, this process could result in an expense for the fund that would be borne by the investors, with a debatable value-add. Venture capital investors are well aware of the potential variability of fair value estimates given the nature of the venture capital investing, which is long-term and is often characterized by binary outcomes (e.g., success or failure).

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Comments on Nonrecurring Fair Value Measurements (Specifically, Nonfinancial Assets & Liabilities in Impairment Tests)

We expect confusion and diversity in practice in applying the disclosure guidance in the proposed ASU, as currently laid out, to nonrecurring measurements. In particular, the assessment of *significance* of the effect of changes in inputs on fair value is ambiguous. There is also a lack of clarity as to how the requirements would be implemented in the context of goodwill impairment tests. Further, since nonfinancial assets are typically interrelated with other assets, the issue of considering and reflecting the interdependencies between reasonably possible inputs becomes even more challenging as the number of inputs that need to be considered further increases, raising a question about the operability of the required disclosure. We have provided a more detailed discussion of the issues that we currently perceive with this aspect of the proposed guidance in the Additional Comments section of this letter.

Duff and Phelps Response to Issue 1, Question 2:

In our experience, few firms have early adopted the revised IFRS 7 guidance. It should be noted that using IFRS 7 guidance as an analogy for implementing the proposed guidance may be flawed for the following reasons:

- a) There may not be a significant *relevant* track record in the application of the revised IFRS 7 disclosure guidance because it has not yet been adopted by the vast majority of companies reporting under IFRS. Therefore it is not yet possible to gauge the real cost and effort required in its implementation.
- b) Because of PCAOB regulation, litigation risk, and SEC oversight, auditors of U.S. GAAP-based financial statements may approach the same set of facts differently than would auditors of IFRS-based financial statements. Therefore the results would differ.
- c) From an alternative investments perspective, IFRS is generally not relevant for most alternative asset investors because of the requirement to consolidate control positions, which does not provide meaningful information to such investors. Therefore there is a limited population of comparable companies that use IFRS. We understand that the proposed ASU is modeled after revised IFRS 7. We support the goal of convergence. However, for the reasons stated above (including in points a) and b)), we do not believe that IFRS 7-type requirements can be adopted in the U.S. through the proposed ASU.
- d) From a nonfinancial assets perspective, because of the nature of such assets, we expect that the cost and effort in implementing the proposed disclosures would be significantly greater.

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Duff and Phelps Response to Issue 1, Question 3:

Comments on Recurring Fair Value Measurements (Alternative Investments)

Based on our discussions with users of financial statements, primarily limited partner investors in alternative assets, we do not believe that most investors would use the information provided through the proposed disclosure.

Certain preparers value a small portion of their portfolio using Level 3 inputs. Therefore, providing a range of value would have little impact on the overall portfolio. In contrast, almost all underlying investments in the private equity sector are valued using Level 3 inputs. A private equity investment partnership typically has a life of 10-15 years. The ultimate investor recognizes that the fair value estimate at the measurement date is just an estimate and the judgment of the general partner who sits on the Board of the portfolio company (companies) is considered to be the best estimate of fair value. Therefore, providing a range of value at the measurement date produces questions about the adequacy of the estimation process for the fair value point estimate, but does not provide incremental decision useful information.

Comments on Nonrecurring Fair Value Measurements (Nonfinancial Assets & Liabilities in Impairment tests)

The result of applying the guidance, as currently proposed, could be an overwhelming amount of disclosures, adding to the complexity of financial statement reports. The usefulness of such disclosures would be a function of the level of disaggregation: they may be meaningful only with a significant level of asset/liability detail which might require disclosures below the asset class level. In order to put the disclosure information in proper perspective, a user would need a basic (and sometimes beyond basic) understanding of the rationale for and application of valuation techniques and inputs in the fair value measurement of various types of assets. As facts and circumstances vary, the use of the appropriate valuation techniques and inputs would also vary, requiring judgment.

Issue 2: With respect to the reconciliation (sometimes referred to as a roll forward) of fair values using significant unobservable inputs (Level 3), the amendments in this proposed Update would require separate disclosure of purchases, sales, issuances, and settlements during the reporting period. Is this proposed requirement operational? If not, why?

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Duff and Phelps Response to Issue 2:

We understand the proposed requirement to be operational.

Issue 3: Is the proposed effective date operational? In particular:

- a. Will entities be able to provide information about the effect of reasonably possible alternative inputs for Level 3 fair value measurements for interim reporting periods ending after March 15, 2010?
- b. Are there any reasons why the Board should provide a different effective date for nonpublic entities?

Duff and Phelps Response to Issue 3:

Comments on Recurring Fair Value Measurements (Alternative Investments)

As noted earlier, it may be very difficult for some preparers to identify reasonably possible alternative inputs for fair value measurements of alternative investments. Therefore, depending on the issuance date, the proposed effective date may be very aggressive.

Comments on Nonrecurring Fair Value Measurements (Nonfinancial Assets & Liabilities in Impairment tests)

Typically, there is a *reasonable range that underlies a valuation analysis*. From this point of view, certain aspects of the information sought by the proposed ASU is already inherent in the valuation analysis supporting a fair value estimate. However, other aspects, such as considering the near-end points of the entire range of possible inputs (*reasonably possible alternative assumptions*) may not be explicitly considered in all valuation analyses. Therefore, it would be costly and inefficient to go back in time and reconstruct the required information after the fact (e.g., after the impairment test has been performed). For example, the analysis supporting a goodwill impairment charge performed in the second fiscal quarter of a March 31 fiscal year-end company would have to be re-opened to provide the required disclosures, as currently laid out in the ASU.

The proposal's issuance date relative to the effective date of the sensitivity disclosures is critical, and should allow the reporting entities sufficient time to identify the information required for disclosure on a timely basis. Some of the fair value measurement analyses for which incremental disclosures would be required are currently ongoing or pending.

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Duff and Phelps Additional Comments

Additional Comments Related to Recurring Fair Value Measurements (Alternative Investments)

The proposed ASU is written from the perspective of single investments valued using one or two inputs. Many financial instruments are valued using multiple inputs and employing multiple techniques. Even under the assumption that only the ends of a reasonable range would be required to be disclosed, and not the exponentially large number of estimates that could be derived using multiple inputs with multiple techniques, the resultant range may provide little decision useful information. Taking the example of a private equity fund that invests in three underlying companies, values could be estimated as follows:

	FV		
	Low	Estimate	High
Portfolio Company A	50	60	100
Portfolio Company B	55	95	100
Portfolio Company C	95	145	200
Total (required disclosure)	200	300	400

The individual data would not be disclosed; only the totals. Therefore the reader of the financial statements would receive \$300 as the point estimate, the exact midpoint of the range, with the range being 33% higher and lower. However, when looking at the underlying data, one company is valued near the bottom of the reasonable range, one at the top and the third slightly below the midpoint. While the individual company data may be of some value, the aggregate range may or may not be of any value. Effectively, the reader of the financial statements receives the following information:

Management believes that if all underlying portfolio companies were sold at the measurement date, the value received would be approximately \$300, however, it is reasonably possible that \$200 would be received or that \$400 would be received or any other amount. That being said, management is not selling the underlying portfolio companies as of the measurement date, but will sell them at some future date when the value could be significantly different.

Unfortunately, the conclusion provided by the hypothetical disclosure may be flawed. Because of the effect of multiple investments in the same portfolio, while it may be reasonably possible that each individual investment could be valued using inputs resulting in the ranges noted above, it is much less likely that it is reasonably possible that all investments would be valued using the low end of their respective ranges or that all investments would be valued using the high end of their respective ranges. Therefore, disclosing \$200 and \$400 as the reasonably possible results for the portfolio of investments is inherently flawed.

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If it is determined that sensitivity disclosures are useful, it may be more beneficial to identify the historical weighted deviation between the fair value estimate and the ultimate realization and then to disclose its impact on value. Assuming that historically, in the aggregate, realizations have deviated from fair value estimates by 10%, the entity would disclose the following:

Management has determined that the fair value estimate of underlying investments at the measurement date is \$300. Historically, ultimate realizations have been within 10% of the most recent fair value estimate, in the aggregate. Based on this historical factor, the range of fair value could be from \$270 to \$330.

Such disclosure would be much closer to reality. It would, however, require preparers to track realizations compared to estimates. Some preparers do this today, but many do not. Therefore there would be an incremental cost related to requiring disclosure using this methodology.

Alternatively, the Board should consider exempting entities who prepare financial statements consistent with ASC Topic 946 (Investment Companies) from the sensitivity disclosure requirement. There are logical reasons for this exemption which include the fact that the use of aggregate ranges provides inherently less reasonably possible outcomes. In addition, investors in investment companies understand that managers exercise informed judgment at each measurement date to identify the best point estimate of fair value. And finally, investors monitor the robustness of the manager's valuation procedures by reviewing quarterly changes in reported value and in assessing realized value compared to last reported fair value.

Additional Comments Related to Nonrecurring Fair Value Measurements (Nonfinancial Assets and Liabilities in Impairment Tests)

Scope & Usefulness of Disclosures

We understand that no disclosures would be required about a fair value measurement unless that measurement is actually *recorded* in the financial statements, which is consistent with the existing requirements of ASC Topic 820. For example, if an indefinite-lived intangible asset is impaired, it will be written down and recorded at its fair value, and in that case the disclosures would apply to this measurement.

This issue becomes more complex in the context of an impairment test for a reporting unit (RU), since the only fair value measurement that would be recorded under paragraph ASC 350-20-35 is the **implied fair value** of goodwill (albeit goodwill can only be measured as a residual).

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Even though the fair value of the RU determined in Step 1 of the goodwill impairment test is used as a de facto purchase price and is assigned to the assets and liabilities of the RU, it is not itself required to be recorded. Similarly, the fair values (or other amounts) of the assets and liabilities of the RU used in determining the implied goodwill are also not recorded on the balance sheet (unless they are impaired and are written down to fair value in accordance with ASC Topics 350 and 360). This raises the question of the usefulness of the disclosures surrounding the fair value estimate of implied goodwill. It may be difficult to put such disclosure into proper context without having information about the fair value of enterprise or equity and the net identifiable assets of the RU, or the total intangible assets of the RU.

Further, it is not clear what the significant inputs in the fair value measurement of implied goodwill might be:

- One interpretation could be that the significant inputs in determining the goodwill are the enterprise value and the fair values (or other amounts) of the net identifiable assets of the RU (goodwill is the difference between the two).
- Another interpretation, perhaps more consistent with some of the illustrations in the proposed ASU, is to consider inputs such as the discount rate.

In light of this, we believe that the scope of the proposed disclosures about nonrecurring fair value measurements (typically related to nonfinancial assets) should be considered more carefully and articulated more clearly. We also recommend that the Board illustrate the application of the proposed disclosures to nonfinancial assets, and specifically in a goodwill impairment situation.

On a related point, we believe that the Board should clarify if the goodwill impairment test in ASC Topic 350 should be performed on an enterprise or on an equity level, as we are aware that there is diversity in practice. The requirements of Topic 350 are unclear, and while we understand that certain interpretations suggest that the test should be performed on an equity level, arguments could be made for the alternative. Clarifying the requirement is necessary as it will affect the nature of the disclosures, i.e., whether a sensitivity analysis should be provided for the enterprise value, the equity value, or both, should the Board or the SEC decide that such disclosures are necessary. Without ample clarifications, the cost of compliance would increase.

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Meaning of Significance

We believe that determining the inputs that have a significant effect on the fair value measurement will be challenging due to the following:

- The articulation of the meaning of *significant* and *significance* is confusing. On one hand, the proposed disclosure requirement in 820-10-50-2(f) focuses on “reasonably possible alternative inputs [that] would increase or decrease **the fair value [measurement]** significantly”, which is based on the individual fair value measurement level. Meanwhile, the benchmark for significance discussed later in 820-10-50-2(f), is based on **earnings and total assets or total liabilities**.
 - If the intent is to *determine significance based on the individual fair value measurement level*, there could potentially be multiple inputs that would significantly affect the fair value measurement, especially in the case of business enterprise and intangible asset valuations. For example, a business enterprise valuation may be significantly impacted by the discount rate, terminal growth rate, EBIT margin, capital expenditure assumptions, etc. Similarly, an identifiable intangible asset, such as a customer relationship, may be significantly impacted by the customer attrition rate, contributory asset charges, margin, discount rate and other assumptions. The contributory asset charge in turn depends on the fair values of other complementary assets. The result could be an overwhelming amount of disclosures and a user may need some understanding of the valuation techniques for various asset classes in order to put the information in perspective.

It should be noted that the interpretation of the meaning of *significance* relating to the *individual fair value measurement* is also consistent with the concept as articulated in ASC Topic 820, which states:

“The level in the fair value hierarchy within which the fair value measurement in its entirety falls shall be determined based on the lowest level input that is **significant to the fair value measurement in its entirety**. Assessing the significance of a particular input to the fair value measurement in its entirety requires judgment, considering factors specific to the asset or liability” [emphasis added].

- If the intent is to *determine significance based on earnings and total assets or total liabilities*, then the question becomes if the effect of the change in a particular input should be considered *in the aggregate* for a group of assets measured at fair value (for example, that might be the case for an impaired asset group tested under ASC Topic 360). While a change in a single key input (e.g. discount rate) may not change the fair value of an individual asset significantly relative to the total assets of the entity, it should be recognized that a variation in that same input may cause a significant change in the fair value measurements of a group of assets when its effect is considered *in the aggregate*.

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Similarly, the effect of the variation in several key inputs may be significant when their impact is considered on the fair value measurements of a group assets *in aggregate*. This is further reinforced by the proposed requirement in the ASU to consider the effects of correlation among changes in significant inputs. As a result, even under this interpretation, there is a potential need to analyze multiple reasonably possible alternative inputs.

In general, since nonfinancial assets are typically interrelated with other assets, the issue of considering and reflecting the interdependencies between inputs becomes even more challenging, raising a question about the operationality of the required disclosure. We also recommend that the Board illustrate the application of the proposed disclosures to nonfinancial assets, including an impaired asset group.

Reasonably Possible Alternative Inputs

As stated earlier, the requirement to consider *reasonably possible* alternative inputs in disclosing the sensitivity of the fair value estimate may result in very wide ranges of value and may have unintended consequences. We believe that the requirement to consider reasonably possible alternative inputs could be narrowed, and be made more operational and useful by considering a range based on *likely alternative assumptions*, or a similar notion. Since the ultimate goal is to provide useful information about a *range of fair values*, we believe that the focus should be more on the *reasonable range that typically underlies any valuation analysis*. Financial reporting requires a single estimate, and therefore only a single point of that range is reported in the financial statements as the fair value measurement; however, that range usually develops as part of the valuation thought process leading to the fair value conclusion.

We observe that a sensitivity analysis of the type proposed in the ASU may be more suited to certain financial instruments. Usually (though certainly not always) financial instruments have fewer interrelationships with other assets, which makes such analysis relatively less complex.

We also note that the usefulness of the proposed disclosures would be a function of the level of disaggregation: the disclosures may be meaningful only with a significant level of asset/liability detail. However, as this may divulge information to competitors this could be of particular concern when it is related to intangible assets, which tend to be unique and proprietary in nature.