

Private Company Financial Reporting Committee

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Judith H. O'Dell CPA CVA
Chair

September 25, 2012

Ms. Leslie Seidman
Chairman
Financial Accounting Standards Board
401 Merritt 7
Norwalk, CT 06856

Re: Proposed Accounting Standards Update, *Disclosures about Liquidity Risk and Interest Rate Risk* (“Proposed ASU”)

Dear Ms. Seidman:

The Private Company Financial Reporting Committee (“PCFRC” or “Committee”) has reviewed the Proposed ASU and focused its attention on those provisions that will affect non-financial institution private companies. The Committee provides its recommendations and comments below in response to certain respondent questions.

Overall, the PCFRC is concerned that the potential benefits of the liquidity risk disclosures are not sufficient when weighed against the cost to private companies of preparing the disclosures. To better balance the cost-benefit equation, the PCFRC recommends that limitations on the required disclosures, perhaps in the form of a triggering mechanism, be introduced into the Proposed ASU. Financial statement user members of the Committee contend that, by and large, they would be aware of a company’s liquidity risks and problems long before the proposed disclosures would reach them. However, users agree that there is some value to liquidity risk disclosures summarized in a cash flow obligations table and an available funds table. Therefore, the PCFRC recommends limiting the proposed disclosures to private companies that are undergoing challenges to their liquidity and are under financial duress¹. Introducing such limitations would greatly narrow the range of private companies that would incur additional cost in preparing the proposed disclosures. At the same time, financial statement users would receive relevant information about cash flow obligations and available funds from those companies that are actually having liquidity problems.

¹ PCFRC members recognize that identifying a triggering mechanism for the proposed disclosures that the management of a company could apply may be problematic.

If the liquidity risk disclosures are required, the PCFRC recommends that they be required only for annual reporting periods and not interim periods for private companies. Given the delayed timing of the receipt of the financial statements by users, the interim data would largely be irrelevant.

Additionally, the PCFRC recommends that the FASB clarify the kinds of cash flow obligations expected to be disclosed by private companies and provide examples to help readers better understand the requirements. Clarity is also needed in defining the term “expected financial cash flow obligations”. Paragraph 825-10-50-23G applicable to financial institutions refers to “financial liabilities” which is defined in the master glossary in the codification as “a contract that imposes on one entity an obligation to do either of the following: a. Deliver cash or another financial instrument to a second entity b. Exchange other financial instruments on potentially unfavorable terms with the second entity.” Paragraph 825-10-50-23M requires an entity that is not a financial institution to provide a “cash flow obligations table.” The term “financial cash flow obligations” is not defined in the glossary and appears to be more broad than a financial liability. See a further discussion of this in our answer to question 2.

Also, as stated in the Committee’s response to Question 20, the PCFRC recommends that the definition of nonpublic entity, as used in the Proposed ASU, include all entities that are not SEC registrants. Following are the Committee’s responses to specific questions posed in the Proposed ASU.

Questions for Preparers and Auditors – Liquidity Risk

Respondent Question 2: *For an entity that is not a financial institution, the proposed amendments would require a cash flow obligations table that includes the expected maturities of an entity’s obligations. Do you foresee any significant operational concerns or constraints in complying with this requirement? If yes, what operational concerns or constraints do you foresee and what would you suggest to alleviate them?*

PCFRC Response: Financial statement preparer and practitioner members of the Committee are concerned that identifying and accumulating the data that underlies the proposed liquidity disclosures will add additional cost, including more audit/review/compilation-related costs, without providing a commensurate benefit to financial statement users (see the response to Question 8). Resources will be spent sifting through accounts in an effort to identify “expected cash flow obligations” of the company for the one to five years (and beyond) presented after the financial statement date.

Additionally, the PCFRC is unclear about what kinds of cash flow obligations will need to be disclosed beyond the examples presented in paragraph 825-10-55-5d of the Proposed ASU. For example, what would be included in “other obligations?” Payroll obligations are a major cash outflow of a typical private company. Are payroll obligations and other obligations such as asset retirement obligations, issued purchase

orders and accounts payable encompassed in the cash flow obligations discussed in paragraph 825-10-50-23M of the Proposed ASU?

The PCFRC recommends that the FASB clarify their intentions about the kinds of cash flow obligations that a private company would be expected to disclose and provide expanded illustrative guidance and examples specific to private companies.

Respondent Question 3: *The proposed amendments would require information about expected maturities for financial assets and financial liabilities to highlight liquidity risk. Expected maturity is the expected settlement of the instrument resulting from contractual terms (for example, call dates, put dates, maturity dates, and prepayment expectations) rather than an entity's expected timing of the sale or transfer of the instrument. Do you agree that the term expected maturity is more meaningful than the term contractual maturity in the context of the proposed liquidity risk disclosures? If not, please explain the reasons and suggest an alternative approach.*

PCFRC Response: The PCFRC recommends that the FASB further clarify the meaning of the term "expected maturity", how a preparer at a non-financial institution private company would operationalize that term, and how it differs from "contractual maturity". Preparers will be required to exercise judgment when applying the term "expected maturity" and reporting inconsistencies could occur when expected cash flow obligations are presented by companies.

Respondent Question 4: *The proposed amendments would require a quantitative disclosure of an entity's available liquid funds, as discussed in paragraphs 825-10-50-23S through 50-23V. Do you foresee any significant operational concerns or constraints in complying with this requirement? If yes, what operational concerns or constraints do you foresee and what would you suggest to alleviate them?*

PCFRC Response: In the private company environment, owner-managers often play a significant role in fulfilling a reporting entity's liquidity needs. The proposed requirements in paragraphs 825-10-50-23S and 23T may present operational concerns to owner-managers who are reluctant to disclose any information related to their ability and willingness to commit funds to a reporting entity.

Respondent Question 6: *As a preparer, do you feel that the proposed amendments would provide sufficient information for users of your financial statements to develop an understanding of your entity's exposure to liquidity risk? If not, what other information would better achieve this objective?*

PCFRC Response: See responses to Questions 2 and 8.

Questions for Users – Liquidity Risk

Respondent Question 8: *Does the cash flow obligations table described in paragraphs 825-10-50-23M through 50-23R provide decision-useful information about*

the liquidity risk of an entity that is not a financial institution? If yes, how would the information provided be used in your analysis of an entity that is not a financial institution? If not, what information would be more useful?

PCFRC Response: The financial statement user members of the PCFRC assert that when a private company has a liquidity problem, users normally are aware of it long before the proposed disclosures would inform them of the problem. Liquidity disclosures are time-sensitive. By the date lenders, sureties, venture capitalists and other users receive financial statements from a private company, such disclosures will lose some relevance. In addition, current analytical measures, such as asset and liability turnover ratios, working capital calculations, and basic indicators of liquidity in the balance sheet, serve users well in providing decision-useful information about liquidity risk. Nevertheless, the user members of the Committee believe that the summarization of liquidity disclosures in a table can be of some assistance in their analyses and decision making. However the additional cost incurred by private companies in complying with the proposed disclosures appear to outweigh the marginal benefits to users.

Further, if a primary goal of the Proposed ASU is to provide financial statement users with information that helps them assess the risk that an entity will encounter difficulty in meeting obligations, then the proposed disclosures about cash flow obligations need to encompass all significant obligations and liabilities that a typical private company would have. The PCFRC is unclear about the kinds of cash flow obligations that should be disclosed beyond the examples provided in paragraph 825-10-55-5d of the Proposed ASU.

To address these concerns, the PCFRC recommends that limitations be placed on which private companies would be required to provide the proposed liquidity disclosures and that the kinds of cash flow obligations expected to be disclosed be clarified in the Proposed ASU. See the beginning of this letter for further elaboration of these recommendations.

Respondent Question 9: *Paragraphs 825-10-50-23S through 50-23V would require an entity to disclose its available liquid funds. Would this table provide decision-useful information in your analysis? If not, what information would be more useful?*

PCFRC Response: Disclosures about available liquid funds, summarized in a table, would be marginally useful information to private company financial statement users. However concern about owner-managers' reluctance to disclose proprietary information, raised in the PCFRC's response to Question 4, will need to be addressed and mitigated.

Respondent Question 10: *Are the proposed time intervals in the tables appropriate to provide decision-useful information about an entity's liquidity risk? If not, what time intervals would you suggest? Do you believe that there are any reasons that these*

required time intervals should be different for financial institutions and entities that are not financial institutions?

PCFRC Response: Some PCFRC members are of the opinion that disclosures about expected cash flow obligations should only be required for two years beyond the financial statement date. Other members believe that such disclosures would be useful for a period of five years beyond the financial statement date. In any event, the PCFRC believes that aggregating three years of expected cash flow obligations (i.e., 20X4-20X6) would be less beneficial than presenting the individual years' obligations.

Additionally, the PCFRC recommends that the FASB clarify its intent with regard to the disclosure of contributions to defined benefit pension plans. The example expected cash flow obligations table presented in paragraph 825-10-55-5d of the Proposed ASU displays dashes (“-”) in the columns beyond one year for the “contributions to defined pension plans” line. However, the Proposed ASU contains no explicit statement that cash flow obligations representing contributions to defined pension plans should only be disclosed for one year. This may be confusing and misleading to readers. The PCFRC recommends that the Proposed ASU limit the disclosure of cash flow obligations for contributions to defined benefit pension plans to one year and explicitly state so.

Respondent Question 11: *With respect to the time intervals, should further disaggregation beyond what is proposed in this Update be required to provide more decision-useful information to the extent that significant amounts are concentrated within a specific period (for example, if a significant amount of liabilities are due in Year 10 of the —past 5 years□ time interval)? Please explain.*

PCFRC Response: See the response to Question 10.

Questions for All Respondents

Respondent Question 20: *The amendments in this proposed Update would apply to all entities. Are there any entities, such as nonpublic entities, that should not be within the scope of this proposed Update? If yes, please identify the entities and explain why.*

PCFRC Response: As stated above, the application of the proposed liquidity disclosures to private companies does not offer sufficient benefit to private company financial statement users when balanced against the cost of implementing the proposed disclosures. As an alternative, the PCFRC recommends that the proposed liquidity disclosures only apply to private companies that meet certain conditions, as stated and further elaborated upon at the beginning of this letter.

Furthermore, the Proposed ASU utilizes the definition of a nonpublic entity found in FASB Codification section 825. That definition is not appropriate in relation to the disclosures contained in the Proposed ASU, especially in view of the fact that the quarterly breakout of the proposed disclosures is relevant only to financial statement

users of SEC registrants. The PCFRC recommends that the definition of nonpublic entity, as used in the Proposed ASU, include all entities that are not SEC registrants.

Respondent Question 21: *Although the proposed amendments do not have an effective date, the Board intends to address the needs of users of financial statements for more information about liquidity risk and interest rate risk. Therefore, the Board will strive to make these proposed amendments effective on a timely basis. How much time do you think stakeholders would require to prepare for and implement the amendments in this proposed Update? Should nonpublic entities be provided with a delayed effective date? If so, how long of a delay should be permitted and why? Are there specific amendments that would require more time to implement than others? If so, please identify which ones and explain why.*

PCFRC Response: While public companies are more accustomed to providing information about an entity's liquidity risks through the preparation of management's discussion and analysis, private companies will need more time to learn about and implement the proposed disclosures. The PCFRC recommends that the effective date of the Proposed ASU be deferred for private companies for a period of one year following the effective date for public companies. Further, the effective date for private companies should be no earlier than December 31, 2013. This delay is recommended for the following reasons:

- A longer lead time is necessary to provide instructors and materials for training a large and broadly distributed audience of private company financial statement preparers, public accountants, and users.
- Third-party resource providers need time to incorporate the proposed disclosures into their products.
- To mitigate the risk that some preparers, public accountants, and to a lesser extent, users of private company financial statements may not become aware of the new guidance.

The PCFRC appreciates the FASB's consideration of this letter. Please feel free to contact me if you have any questions or comments.

Sincerely,



Judith H. O'Dell
Chair
Private Company Financial Reporting Committee

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