Notice for Recipients
of This Proposed FASB Staff Position

This proposed FASB Staff Position (FSP) amends FASB Statement No. 157, *Fair Value Measurements,* to provide application guidance for estimating the fair value of investments in investment companies that have calculated net asset value per share in accordance with the AICPA Audit and Accounting Guide, *Investment Companies.*

The Board invites individuals and organizations to send written comments on all matters in this proposed FSP. Respondents need not comment on all of the issues presented and are encouraged to comment on additional issues as well. Comments are requested from those who agree with the provisions of this proposed FSP as well as from those who do not. Comments are most helpful if they identify the issues to which they relate and clearly explain the reasons for the positions taken. Those who disagree with provisions of this proposed FSP are asked to describe their suggested alternatives, supported by specific reasoning.

The Board requests that constituents provide comments on the following questions:

1. This proposed FSP would apply to an investment in an entity that meets the definition of an investment company in the investment companies Guide for which its net asset value per share (or its equivalent, for example, partners' capital per share for an investment in a partnership) has been calculated in accordance with that Guide. However, this proposed FSP would not apply if the fair value of the investment is readily determinable as defined in paragraph 3 of FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities* (with one exception described in paragraph 13 of this proposed FSP). Do you believe there are other investments that should be within the scope of this proposed FSP? If so, what principle should be used to determine which investments are within the scope of the proposed FSP? Do you agree that the Board should not permit the

application of the proposed FSP to investments in entities that have readily determinable fair values as defined in paragraph 3 of Statement 115? Are there other investments that the Board should exclude from the scope of this proposed FSP?

2. Are there circumstances in which an investment might initially have a readily determinable fair value and in a subsequent period not have a readily determinable fair value (and thus arguably become eligible for the practical expedient)? If so, please describe those circumstances. In those circumstances, should the investment be eligible for the practical expedient even though the investor may not be able to transact with the investee (fund) at net asset value per share?

3. The Board also considered alternative approaches to the scope of this proposed FSP. One approach would have indicated that a condition to using the practical expedient is that the primary means to enter and exit the investment is transactions (for example, redemptions or distributions) between the investor and the investee (that is, the fund) at net asset value per share. Another approach would have indicated that a condition to using the practical expedient is that the principal or most advantageous market for the investment is transactions (for example, redemptions or distributions) between the investor and the fund at net asset value per share. Do you believe the Board should pursue one of the alternative approaches instead of the approach taken in this proposed FSP? If so, why?

4. The Board recognizes that permitting rather than requiring the application of this proposed FSP for entities within its scope potentially reduces comparability. The Board decided to permit rather than require that reporting entities apply this proposed FSP to investments within its scope, in part, to avoid potential conflicts with the "good faith" requirements of the Investment Company Act of 1940 and Accounting Series Releases No. 113, *Statement Regarding "Restricted Securities,"* and No. 118, *Accounting for Investment Securities by Registered Investment Companies.* Do you agree with the

Board's decision to permit rather than require the application of this proposed FSP? Are there any other unintended consequences of requiring the application of this proposed FSP to investments within its scope?

5. Are the disclosure requirements of this proposed FSP operational? Should the Board require all of the disclosure by major category (or should it permit some of them on a more aggregated basis)? If the final FSP is effective upon issuance (for example, assume issuance is July 31, 2009), can the disclosures be provided for prior periods for which financial statements have not been issued? Are there other disclosures that the Board should consider requiring?

Responses must be received in writing by July 8, 2009. Earlier responses are encouraged. Interested parties should submit their comments by email to director@fasb.org, File Reference: Proposed FSP FAS 157-g. Those without email may send their comments to "Technical Director, FASB, 401 Merritt 7, PO Box 5116, Norwalk, CT 06856-5116, File Reference: Proposed FSP FAS 157-g." Responses should not be sent by fax. All comments received by the FASB are considered public information. Those comments will be posted to the FASB website and included as part of the project record with other project materials.

PROPOSED FASB STAFF POSITION

No. FAS 157-g

Title: Estimating the Fair Value of Investments in Investment Companies That Have Calculated Net Asset Value per Share in Accordance with the AICPA Audit and Accounting Guide, *Investment Companies*

Date Released: June 8, 2009

Comment Deadline: July 8, 2009

Objective

1. This proposed FASB Staff Position (FSP) amends FASB Statement No. 157, *Fair Value Measurements,* to provide application guidance for estimating the fair value of investments in investment companies that have calculated net asset value per share in accordance with the AICPA Audit and Accounting Guide, *Investment Companies*.

Background

2. Statement 157 establishes a single definition of fair value and a framework for measuring fair value in generally accepted accounting principles that result in increased consistency and comparability of fair value measurements. Statement 157 also expands disclosures about fair value measurements. Statement 157 does not require any new fair value measurements.

3. The FASB obtained extensive input from various constituents, including financial statement users, preparers, and auditors, on determining fair value in accordance with Statement 157. Many of those constituents indicated that the fair value measurement framework in Statement 157 and related disclosures have improved the quality and transparency of financial information. However, some constituents have requested additional authoritative guidance on the application of Statement 157.

4. An investor may make investments in entities (investees) that permit the investor to redeem the investment directly with or receive distributions from the investee at net asset

value per share at times allowable under the terms of the investee's governing documents. Many of these investments do not have readily determinable fair values (that is, investments that are not listed on national exchanges or over-the-counter markets such as the National Association of Securities Dealers Automated Quotation System). Examples of these investees (also referred to as "alternative investments") include hedge funds, private equity funds, real estate funds, venture capital funds, offshore fund vehicles, and funds of funds. Many of these investees provide their investors with a net asset value per share[1] (or its equivalent, for example, partners' capital per share if the investee is a partnership) that has been calculated in accordance with the investment companies Guide. Among other requirements, that Guide indicates that in arriving at the investee's net asset value per share, the investee must measure all of its underlying investments at fair value in accordance with Statement 157.[2]

5. If there is no readily determinable fair value, it is common practice for investors to estimate the fair value of their investment using its net asset value per share without further adjustment. In some cases this is because the investee regularly stands ready (without significant restriction) to redeem the investment for net asset value per share

---

[1]Paragraph 7.39 of the investment companies Guide defines net asset value per share as follows:

> Net asset value per share is the amount of net assets attributable to each share of capital stock (other than senior equity securities, that is, preferred stock) outstanding at the close of the period. It excludes the effects of assuming conversion of outstanding convertible securities, whether or not their conversion would have a diluting effect. Net asset value per share should be disclosed for each class of shares.

[2]Paragraph 1.06 of the investments companies Guide indicates the following:

> Investment companies discussed in this guide are required to report their investment assets at fair value, as defined by Financial Accounting Standards Board (FASB) Statement No. 157, *Fair Value Measurements*, and have the following attributes:
>
> *a.* *Investment activity*. The investment company's primary business activity involves investing its assets, usually in the securities of other entities not under common management, for current income, appreciation, or both.
> *b.* *Unit ownership*. Ownership in the investment company is represented by units of investments, such as shares of stock or partnership interests, to which proportionate shares of net assets can be attributed.
> *c.* *Pooling of funds*. The funds of the investment company's owners are pooled to avail owners of professional investment management.
> *d.* *Reporting entity*. The investment company is the primary reporting entity. [Footnote reference omitted.]

and, thus, net asset value per share is a good indication of the price the investor would receive to sell its investment (fair value). If there are restrictions to redemption or the investment is designed for redemption to occur through distributions from the investee, many investors indicated that they believe that the key consideration when relying on net asset value per share without further adjustment is that the investee's underlying investments are reflective of fair value as defined by Statement 157 at the investor's measurement date. However, some constituents have expressed concern that net asset value per share may not represent the fair value of the investment in all circumstances. They maintain that certain features of the investment may warrant making adjustments to net asset value per share to estimate the fair value of the investment.

6. In January 2009, the AICPA Accounting Standards Executive Committee and the Alternative Investments Task Force issued a draft Issues Paper, "FASB Statement No. 157 Valuation Considerations for Interests in Alternative Investments." The draft paper includes nonauthoritative guidance on estimating the fair value of investments in certain alternative investments. The draft paper indicates that when estimating fair value, an investor must consider other attributes and features of the investment in addition to the investee's net asset value per share. Those considerations include contractual attributes of the investment such as redemption restrictions (for example, lockups and gates) and unfunded commitments, the intangible benefits of the investment (for example, access to certain types of investments or investment strategies), and the presence of principal-to-principal or brokered transactions for the investment.

7. The FASB staff reviewed comment letters received by the AICPA on the draft paper. Additionally, the FASB staff held discussions about the valuation of alternative investments with various constituent groups, including financial statement users, auditors, and preparers. Many constituents expressed concerns about several aspects of the draft paper. Those constituents asserted that the draft paper lacks sufficient clarity about which features of the investment require an adjustment to net asset value per share and whether an adjustment would be an increase or decrease to net asset value per share. They stated that some adjustments may be increases to net asset value per share (for example, for access to certain types of investments or investment strategies and for access

to a particular investment manager). Other adjustments, such as the imposition of a gate, may be decreases to net asset value per share (for example, for preventing an otherwise redeemable interest in an investment from being redeemed for a period of time). However, some constituents stated that gates may provide a benefit to investors (for example, the imposition of a gate prevents the investment manager from being required to sell the investee's underlying investments in a disorderly transaction).

8. Some constituents also asserted that the draft paper places too much emphasis on principal-to-principal or brokered transactions as observable inputs to a fair value measurement. Those constituents indicated that principal-to-principal or brokered transactions for the types of investments within the scope of this FSP are uncommon and that those transactions often involve a distressed seller. Consequently, in their view, in most circumstances principal-to-principal or brokered transactions are not relevant observable inputs to a fair value measurement of an alternative investment within the scope of this FSP because the investment is designed (a) to be redeemed with the investee or (b) to be exited via distributions from the investee at times allowable under the terms of the investee's governing documents.

9. The Board decided that net asset value per share is the most relevant estimate of fair value available that would not require undue cost and effort for investments within the scope of this FSP. In the Board's view, on balance, the cost and effort involved in evaluating (a) the specific features of the investment (including any intangible benefits) and (b) any principal-to-principal or brokered transactions for an investment within the scope of this FSP outweigh any benefits. The Board received input from financial statement users indicating that highly subjective adjustments to net asset value per share do not provide the most decision-useful information. Instead, financial statement users indicated that they generally prefer the comparability of net asset value per share without further adjustment. They also suggested requiring additional disclosure about the features and attributes of these investments, such as the nature of any restrictions on the investor's ability to redeem its investment and any unfunded capital commitments.

10. As a practical expedient, the Board decided that a reporting entity should be permitted to estimate the fair value of an investment within the scope of this FSP using net asset value per share (or its equivalent, for example, partners' capital per share for an investment in a partnership) without further adjustment, if the net asset value per share of the investment is determined in accordance with the investment companies Guide as of the reporting entity's measurement date.

11. This FSP does not provide guidance for determining net asset value per share in accordance with the investment companies Guide. It also does not provide guidance for determining the procedures that the reporting entity performs to determine whether net asset value per share was determined in accordance with that Guide as of the reporting entity's measurement date. The following are examples of guidance that may be useful in making those determinations and performing those procedures:

a. The investment companies Guide and AICPA Technical Practice Aid, TIS Section 6910, *Investment Companies,* paragraph 29, "Allocation of Unrealized Gain (Loss), Recognition of Carried Interest, and Clawback Obligations"
b. Statement on Auditing Standards No. 92 (AU Section 332), "Auditing Derivative Instruments, Hedging Activities, and Investments in Securities" and Auditing Interpretations of Section 332 (AU 9332), "Auditing Investments in Securities Where a Readily Determinable Fair Value Does Not Exist"
c. The 2006 AICPA Technical Practice Aid, "Auditing Alternative Investments."

All paragraphs in this FSP have equal authority.
Paragraphs in bold set out the main principles.

FASB Staff Position

Scope

12. This FSP applies to investments in entities that meet the definition of an *investment company* in paragraph 1.06 of the investment companies Guide for which the entity's net asset value per share (or its equivalent, for example, partners' capital per share for an investment in a partnership) has been calculated in accordance with that Guide. However, this FSP does not apply if the fair value of the investment is readily

determinable as defined in paragraph 3 of FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities.* For example, this FSP does not apply to an investment in a registered, closed-end investment company whose fair value can be estimated using sales prices that are currently available on a securities exchange registered with the Securities and Exchange Commission or in an over-the-counter market, provided that those prices or quotations for the over-the-counter market are publicly reported by the National Association of Securities Dealers Automated Quotation System or by Pink Sheets LLC.

13. For purposes of applying paragraph 12 of this FSP, a restriction of greater than one year in length on a reporting entity's ability to sell an investment shall not be considered when determining whether the fair value of the investment is readily determinable.

14. The following are examples of authoritative accounting pronouncements that permit or require a fair value measurement of an investment to which a reporting entity may apply this FSP if the investment is within the scope of the FSP:

a. The investment companies Guide (for example, when a reporting entity within the scope of that Guide invests in another entity within the scope of the Guide)
b. FASB Statement No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities*
c. The AICPA Audit and Accounting Guide, *Not-for-Profit Organizations* (for example, for the subsequent fair value measurement of an investment when the reporting entity elects fair value as the subsequent measurement attribute or when testing for other-than-temporary impairment if the investment is subsequently measured at cost or using the equity method)
d. APB Opinion No. 18, *The Equity Method of Accounting for Investments in Common Stock*, EITF Topic No. D-46, "Accounting for Limited Partnership Investments," or other equity method guidance (for example, for an other-than-temporary impairment analysis of an equity method investment)
e. FASB Statements No. 35, *Accounting and Reporting by Defined Benefit Pension Plans*, and No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans*, or other benefit plan guidance
f. FASB Statement No. 107, *Disclosures about Fair Value of Financial Instruments*.

Measurement

15. **In circumstances in which net asset value per share of an investment is not determinative of fair value, a reporting entity is permitted, as a practical expedient, to estimate the fair value of an investment within the scope of this FSP using the net asset value per share of the investment (or its equivalent, for example, partners' capital per share for an investment in a partnership) without further adjustment, if the net asset value per share of the investment is determined in accordance with the investment companies Guide as of the reporting entity's measurement date.**

Disclosures

16. If an investment is within the scope of this FSP, for both recurring and nonrecurring measurements, a reporting entity shall disclose information that enables users of its financial statements to understand the nature and risks of the investment. To meet that objective, to the extent applicable, the reporting entity shall disclose the following information for each interim and annual period separately for each major category of investment (Major category shall be determined on the basis of the nature and risks of the investment.):

a. The fair value (determined by applying this FSP, if applicable) of investments within the scope of this FSP, separately disclosing the fair value of investments to which the reporting entity has applied the practical expedient in paragraph 15 of this FSP, and a description of the significant investment strategies of the investee(s).
b. The reporting entity's best estimate of the remaining life of a finite lived investment.
c. The amount of the reporting entity's unfunded commitments related to its investment.
d. The terms and conditions upon which the investor may redeem its investment (for example, quarterly redemption with 60 days' notice).
e. The circumstances in which an otherwise redeemable investment (or a portion thereof) might not be redeemable (for example, due to a lockup or the imposition of a gate). Also, for those otherwise redeemable investments that are restricted from redemption as of the reporting entity's measurement date, the reporting entity shall disclose its best estimate of when the restriction against redemption might lapse.
f. Any other significant restriction on the ability to redeem or sell the investment at the measurement date.

Effective Date and Transition

17. This FSP shall be effective upon issuance, including prior periods for which financial statements have not been issued, and applied prospectively. This FSP does not require disclosures for earlier periods presented for comparative purposes at initial adoption. In periods after initial adoption, this FSP requires comparative disclosures only for periods ending after initial adoption.

18. A revision resulting from a change in valuation technique or its application shall be accounted for as a change in accounting estimate (FASB Statement No. 154, *Accounting Changes and Error Corrections,* paragraph 19). The disclosure provisions of Statement 154 for a change in accounting estimate are not required for revisions resulting from a change in valuation technique or its application.

The provisions of this FSP need not be applied to immaterial items.

Appendix

AMENDMENTS TO STATEMENT 157

A1. Statement 157 is amended as follows: [Added text is underlined.]

a. Paragraphs 31B–31D and their related heading are added as follows:

***Estimating the Fair Value of Investments in Investment Companies That Have Calculated Net Asset Value per Share in Accordance with the AICPA Audit and Accounting Guide*, Investment Companies**

31B. The guidance in paragraph 31D shall apply only to investments in entities that meet the definition of an investment company in paragraph 1.06 of the AICPA Audit and Accounting Guide, *Investment Companies*, for which the entity's net asset value per share (or its equivalent, for example, partners' capital per share for an investment in a partnership) has been calculated in accordance with that Guide. However, the guidance in paragraph 31B shall not apply if the fair value of the investment is readily determinable as defined in paragraph 3 of FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*. For example, this paragraph does not apply to an investment in a registered, closed-end investment company whose fair value can be estimated using sales prices that are currently available on a securities exchange registered with the Securities and Exchange Commission or in an over-the-counter market, provided that those prices or quotations for the over-the-counter market are publicly reported by the National Association of Securities Dealers Automated Quotation System or by Pink Sheets LLC.

31C. For purposes of applying paragraph 31B, a restriction of greater than one year in length on a reporting entity's ability to sell an investment shall not be considered when determining whether the fair value of the investment is readily determinable.

31D. In circumstances in which net asset value per share of an investment is not determinative of fair value, a reporting entity is permitted, as a practical expedient, to estimate the fair value of an investment within the scope of paragraph 31B using the net asset value per share (or its equivalent) of the investment without further adjustment, if the net asset value per share of the investment is determined in accordance with the investment companies Guide as of the reporting entity's measurement date.

b. Paragraph 33A is added as follows:

33A. If an investment is within the scope of paragraph 31B, for both recurring and nonrecurring measurements, a reporting entity shall disclose information that enables users of its financial statements to understand the nature and risks of the investment. To meet that objective, to the extent applicable, the reporting entity shall disclose the following information for each interim and annual period separately for each major category of investment (Major category shall be determined on the basis of the nature and risks of the investment.):

a. The fair value (determined by applying paragraph 31D, if applicable) of investments within the scope of paragraph 31B, separately disclosing the fair value of investments to which the reporting entity has applied the practical expedient in paragraph 31D, and a description of the significant investment strategies of the investee(s).
b. The reporting entity's best estimate of the remaining life of a finite lived investment.
c. The amount of the reporting entity's unfunded commitments related to its investment.
d. The terms and conditions upon which the investor may redeem its investment (for example, quarterly redemption with 60 days' notice).
e. The circumstances in which an otherwise redeemable investment (or a portion thereof) might not be redeemable (for example, due to a lockup or the imposition of a gate). Also, for those otherwise redeemable investments that are restricted from redemption as of the reporting entity's measurement date, the reporting entity shall disclose its best estimate of when the restriction against redemption might lapse.
f. Any other significant restriction on the ability to redeem or sell the investment at the measurement date.