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

February 29, 2016

Re: **File Reference No. 2015-350**; Exposure Draft – *Disclosure Framework - Changes to the Disclosure Requirements for Fair Value Measurement*

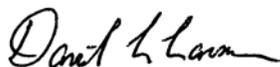
Dear Technical Director:

Duff & Phelps appreciates the opportunity to provide comments on the above referenced exposure draft.

Our valuation advice, particularly with regards to financial reporting, is sought by hundreds of global clients annually as we work with them in developing pragmatic solutions for applying fair value techniques. We believe that our unique perspective in the practical application of valuation principles has particular relevance to the FASB and its constituency.

We would be pleased to further discuss our comments with the FASB Staff. Please direct any questions to me via the contact information set forth below.

Sincerely,



David Larsen  
Managing Director,  
Valuation Advisory Services

DUFF & PHELPS

FASB

February 29, 2016

Fair Value Measurement (Topic 820)  
Disclosure Framework – Changes to  
the Disclosure Requirements for Fair  
Value Measurement

# General Observations

## General Observations

We appreciate FASB's efforts in continuing to improve the Conceptual Framework for financial reporting, and in testing the guidance in the proposed *FASB Concepts Statement – Chapter 8: Notes to Financial Statements* by applying it to fair value measurements.

We have set forth below a few observations on the *Exposure Draft: Disclosure Framework – Changes to the Disclosure Requirements for Fair Value Measurements* ("ED") from the perspective of valuation specialists with extensive experience working with Alternative Investment Managers and Investors who report and use fair value information.

## Disclosures about "Level 0" Measurements

As FASB is refining the fair value measurement disclosures, we think it should give consideration to the manner of disclosure of certain practical expedients. Under ASU 2015-07, investments measured at net asset value ("NAV") as a practical expedient are excluded from the fair value hierarchy, which leaves a gap in the presentation, as the aggregate of the fair value hierarchy disclosures (Levels 1, 2 and 3) does not reconcile to the total of investments measured at fair value on the balance sheet.

These NAV practical expedients are effectively "Level 0" measurements. We think that a more consistent picture of fair value measurements in the disclosures would be painted by including these "Level 0" measurements in the same place as the rest of the fair value disclosures which are subject to the fair value hierarchy. Further, this would help juxtapose NAV measurements that are practical expedients with NAV measurements that are in fact fair value measurements and should therefore be classified in Levels 2 or 3.

## Range, Weighted Average and Time Period used for Unobservable Inputs

We believe that the disclosures about the *range, weighted average and time period used* in developing significant unobservable inputs (par. 820-10-50-2-bbb) is not meaningful for all fair value measurements: For example:

- These proposed disclosures are not meaningful for private equity (PE) and venture capital (VC) investments. Each investment is unique, and as such, ranges and averages, even weighted averages, do not convey meaningful information about the investments either individually or as an asset class.

- Similarly, we do not believe that these disclosures are meaningful or useful for many nonfinancial assets<sup>1</sup>. Nonfinancial assets, and particularly intangible assets, tend to be unique and therefore generalizations and comparisons across companies may not be meaningful for investors, especially without having the proper valuation context about the remaining related assets in the subject asset group/business.
- Further, as a general matter, an input might not always *on its own* convey the information it purports to convey. For example, a disclosure of the discount rate does not unequivocally indicate the risk of the investment (as described in BC 46); rather, it provides an indication of the risk inherent in the *projections* to which the discount rate was applied.  
  
For example, one can analyze the same investment and apply a high discount rate if using conditional or optimistic cash flows (Discount Rate Adjustment Technique), but apply a lower discount rate if using expected cash flows (Expected Present Value Technique). A reader focusing on the disclosure of the discount rate as a significant unobservable input may have very different takeaways when faced with the two different ranges that would underlie the two techniques as applied to the same investment and resulting in the same fair value. (The choice of discount rate input in the analysis depends on the available relevant data, technique used, reliability of cash flows, industry practice and a host of other factors.)
- Also, the reader may (correctly) expect a relationship between the disclosed range of unobservable inputs and their effect on the measurement uncertainty of the concluded fair value. However, the relationship may not be proportionate across the significant unobservable inputs disclosed with respect to a particular fair value measurement. Varying certain significant inputs may have a greater impact on the concluded fair value than the variation of other significant inputs which may have a smaller impact. In other words, the width of the range around a significant unobservable input does not directly translate into the same order of magnitude of measurement uncertainty around the concluded fair value.

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<sup>1</sup> We understand that the changes proposed to paragraphs 820-10-50-2-bbb would also apply to Level 3 nonrecurring fair value measurements. The proposed disclosures would be required when, for example, certain nonfinancial assets are written down to fair value in an impairment test.

This issue is further compounded by the aggregation of assets - and especially by the aggregation of assets with nonhomogeneous characteristics.

In summary, we think that the Board should reconsider the usefulness of some of the required disclosures in light of the comments above. Also, we believe that the types of fair value disclosures proposed in the ED (range, weighted average and time period used to develop significant unobservable inputs) are more meaningful when applied to pools of homogeneous assets, subject to our comments above.

### Change in Unrealized Gains and Losses

We note that the new requirement to disclose unrealized gains and losses arising from recurring measurements disaggregated by Level (Levels 1 and 2, in addition to Level 3) is not meaningful for PE and VC investments. Disaggregating unrealized gains and losses by level inadvertently may cause readers to assume that the quality of the asset and hence the reliability of the unrealized gain or loss is somehow tied to the inputs used to determine fair value. The level of valuation inputs is not pertinent to the quality of the underlying asset being fair valued.

In particular, investors in Alternative Assets are focused on the aggregate unrealized gain/loss for each period and do not track or make decisions based on unrealized gains/losses resulting from the input level used to reach the fair value conclusion.

### Measurement Uncertainty Disclosures

While changing the description of the disclosure in par. 820-10-50-2g from a *sensitivity analysis* to a *measurement uncertainty analysis as of the reporting date* may clarify the intended nature of the disclosure (a current, rather than a prospective view of uncertainty/sensitivity), we think that this does little to make the disclosure truly meaningful.

Further, we think that the illustration of the discussion of measurement uncertainty in par. 820-10-55-106 does not provide much useful information. This is the kind of disclosure that could be described as being obvious to a reasonably informed user. Therefore, this illustration also brings into question the usefulness of the required measurement uncertainty disclosures in par. 820-10-50-2g.

Aside from this, we continue to believe that the fair value framework provides the most decision-useful information for users of financial statements, especially with respect to alternative investment managers and investors. However, significant informed judgment is required to

estimate fair value, especially when using Level 3 inputs. As such, while the accounting framework requires a point estimate, there is generally a reasonable range surrounding the point estimate. In some circumstances, the reasonable range may be wide, and in fact may exceed deemed materiality. In addition, individual fair value ranges, when aggregated, may be exceedingly wide. Unfortunately, this reality does not readily lend itself to disclosure that effectively balances usefulness with operationality and cost effectiveness.

### Assets and Liabilities for which Fair Value is Only Disclosed

We suggest that FASB consider further simplifying the disclosure requirements in par. 820-10-50-2E which address assets and liabilities not measured at fair value in the statement of financial position, but for which fair value is disclosed. For example, whether the highest and best use of a nonfinancial asset for which fair value is only disclosed differs from its current use may not provide very useful information.

### Illustration of Proposed Disclosures – Valuation techniques and Inputs

While this is unrelated to the details of the proposed disclosures, we noticed that the illustration provided in par. 820-10-55-103 could be construed to imply that control premiums and discounts for lack of marketability are *always* appropriate for PE and VC investments. This is not the case. And since the Accounting Standards Codification is an authoritative source of U.S. GAAP, we are concerned that readers will take this illustration in par. 820-10-55-103 too literally and always expect a control premium or a marketability discount when valuing PE and VC investments. In order to avoid perpetuating a serious misconception, we recommend that FASB change the ranges presented to include zero as the low end of these input ranges.

The view that control premiums and discounts for lack of marketability can be zero in some cases is also consistent with the leading practices in the valuation of PE and VC investments. These views are being documented in a new AICPA Accounting & Valuation Guide, currently in development, which is focused on the investment industry.

Another misconception that might be perpetuated via the illustration in par. 820-10-55-103 is that VC investments are valued by a discounted cash flow approach (DCF), which is rarely the case. The use of the DCF approach is implied by the reference to the weighted average cost of capital (WACC) in the table in par. 820-10-55-103. Further, if projections are used with VC investments, they are discounted at rates that are not

typically derived as a WACC, but can be characterized as being based on the Discount Rate Adjustment Technique described in ASC 820, which requires an analysis of market rates associated with conditional cash flows, including a build-up approach.

### Private Company Simplifications & Disclosure Exemptions

While the FASB and PCC have focused on simplifying a number of financial reporting requirements for private companies - including those related to fair value measurement disclosures in the ED - the fact is that private companies may be more dissimilar than they are similar, notwithstanding the general “private company” label.

Shareholders may have different needs depending on the circumstances of the private company they invest in. For example, there are a number of late-stage private companies – from the relatively smaller ones to the unicorns of the world - which have minority investors with information needs that might be better served by public company GAAP. These are essentially pre-public investments that are a permanent fixture in a well-developed capital market, and which are much closer to public companies than they are to small closely-held private companies in their characteristics and prospects. Yet the reality is that minority investors in these pre-public companies do not always have the direct access to management that presumably comes with being an investor in a closely held (and smaller) private company. The needs of these investors could be met with better quality, quantity and timeliness of information (including disclosures), rather than by less information, especially considering the risk of changing conversion rates for their investments that these investors bear as an IPO nears.

As such, we think that as a general matter, FASB should give greater consideration to the varying information needs of different private company shareholders, recognizing that not all private companies and private company investors share similar traits and have similar needs.