

December 4, 2017

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

Reference: Technical Director, File Reference No. 2017-320

Dear Technical Director:

Duff & Phelps is pleased to provide a response to the proposed Accounting Standards Update (Proposed ASU) on Codification Improvements. 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.

Our comments are limited to **Issue 14**.

Question 1

Do you agree with the amendments to the Codification in this proposed Update? If not, please explain which proposed amendment(s) you disagree with and why.

Response

We agree with the proposed amendments on Issue 14 on the basis that the Board has previously deliberated the issue, followed due process, and has concluded on certain measurement principles. We understand that the current language of the FASB Accounting Standards Codification with respect to the treatment of restrictions on the sale of an asset when measuring a corresponding liability or equity interest is not aligned with the Board's decision at the time, and the amendments are meant to clarify those decisions. However, we have a few observations, set forth below.

We are concerned about divergence with IFRS, since par. 39 of IFRS 13 contains language that is identical to the current language in the Codification. Considering that the Proposed ASU is essentially correcting and clarifying the current language in the U.S. GAAP fair value standard, this may lead to inconsistency in conforming with the two standards. Without conforming amendments to IFRS 13, two cornerstone standards in IFRS and U.S. GAAP will start diverging. We believe it is critical to maintain convergence between the two fair value measurement standards.

Additionally, we recommend that the Board more clearly articulate the rationale for not adjusting the price of the asset for a restriction on its sale, either in the text of the amendments or in the Basis for Conclusions of a final ASU, and include illustrations as well.

- For example, currently, the discussion in par. 41 a. and b. of the Proposed ASU does not address the issue directly, in that 41 a. only makes clear that a restriction on an entity's ability to transfer a liability (or equity instrument) is not included as an adjustment to the price of the corresponding asset; whereas 41 b. only reiterates an asset fair value measurement principle, which considers if a restriction is an attribute of the asset or not in determining whether an adjustment is needed to the price of the asset.

What is still needed is an explanation as to why - or in what circumstances - is it appropriate to reflect the restriction on the sale of the asset in the valuation of the liability.

On a conceptual level, however, we observe that the conclusion that the price of the liability should equal that of a corresponding asset ignores the principal market notion, as well as the notion that a liability (or equity instrument) is priced in a transfer to a market participant. Thus, pricing the liability based on a corresponding asset appears to be a practical expedient.

A few additional observations:

- We understand that the proposed amendment may be addressing the situation in which an instrument classified in a reporting entity's shareholders' equity relates to interests issued as consideration in a business combination, whereby the seller receives restricted stock, and the restriction is an attribute of the asset. In this case, following the current Codification guidance in ASC 820-10-35-16D could lead one to exclude the restriction on the sale of the asset, which may "overvalue" the consideration paid.

However, it could be argued that the buyer of the business is sacrificing/transferring an asset in exchange for the business (interest) acquired, and the transaction price of the asset given up is more clearly evident (logically leading one to reflect the restriction on the sale of the asset in the valuation of the instrument classified in equity). This might be a different way of explaining how one may get to the "correct" conclusion in the measurement of an instrument classified in the entity's shareholders' equity.

- If the argument is that the restriction on the sale of the asset is priced into the corresponding liability or equity instrument (which are therefore measured by reference to the asset), then the question becomes whether only restrictions that are considered attributes of the asset under ASC 820 are in fact negotiated into the terms and pricing of these types of transactions.

Is it possible in certain circumstances for the liability or instrument classified in shareholders' equity to represent a different unit of account from the asset, and to reflect restrictions on sale that are not considered to be characteristics of the asset (e.g., a restriction on the asset holder, such as the case with a Board seat), but are nonetheless part of the arrangement? (If the Board has already addressed this, it would be helpful if the discussion is incorporated in the Basis for Conclusions of the final ASU, when issued.)

Perhaps entity-specific features on the asset side could still be considered market participant characteristics of the liability (or instrument classified in shareholders' equity) under certain circumstances.

- To illustrate a similar notion, consider a business combination where the buyer expects to realize certain entity-specific synergies. The buyer also has a contingent consideration arrangement in place which is based on achieving certain combined entity-specific milestones.

Only market participant synergies, but not entity-specific synergies would be reflected in the valuation of the business and the acquired assets and assumed liabilities in the purchase price allocation under ASC 820. However, in measuring the contingent consideration liability at fair value, the specified milestones become attributes of the liability and would transfer to a market participant as part of the liability (contingent consideration contract). As such, these entity specific synergies would be considered in the valuation of the contingent consideration liability, but not in the valuation of the assets, liabilities and the overall business acquired.

Based on the above discussion, would the measurement principle be better described as follows – a restriction on the sale of the asset (*or holder*) would be reflected in the measurement of the corresponding liability when market participants would also consider it when pricing the liability – rather than fixing the measurement of the liability to the *asset*, and focusing on whether the restriction is an attribute of the *asset*. (And would a similar principle apply to an instrument classified in shareholders' equity with a corresponding asset?)

Separately and more broadly, a liability is generally associated with performance, sacrifice of resources, and other assumptions that are *liability-centric*.

- For example, taxes are usually believed to not affect the amount of the performance obligation (would not diminish the value of the obligation), even if the expenses incurred in fulfilling the liability are tax deductible. The argument is that this does not affect the *performance or fulfillment* effort per se, and a market participant would not accept a lower amount to assume a liability because of consideration of taxes in this case.

The issue of restrictions on the sale of an asset that corresponds to a liability might fall into a similar line of reasoning – as the restriction is on the asset, not on the liability – one must adopt a liability-centric view in the measurement. Additionally, as stated earlier, the fair value measurement framework is rather specific as to the steps taken in identifying the principal market, market participants and all other elements that would be considered in a fair value measurement. The outcome may very well be that in some circumstances, the conclusion is that the fair value of the liability does equal the fair value of the asset inclusive of the restriction (that is an attribute of the asset), but this should not be considered a foregone conclusion.

Perhaps the premise that the fair value of the liability (or equity instrument) may equal the corresponding asset is limited to financial instruments, in specific circumstances. As such, pegging the measurement of the liability to the asset (inclusive of restrictions) may appear to be more of a practical expedient, against the background of fair value measurement of liabilities generally which follows the ASC 820 fair value measurement framework.

The valuation of liabilities is a complex area and little guidance exists on the topic. We understand that guidance may continue to evolve. Additionally, the Board should be advised that the IVSC may take on a project to develop a standard for the valuation of liabilities for a variety of valuation purposes.

Question 2

Would any of the proposed amendments result in substantive changes to the application of existing guidance that would require transition provisions? If so, please describe?

Response

We are aware of certain interpretations in practice that reflect the current wording of the Codification – i.e., that the effect on restrictions on the sale of the asset are reversed from the valuation of the corresponding liability. It is difficult to assess how wide-spread this interpretation is and how much it has affected practice.

Question 3

Are there other changes that should be made that are directly or indirectly related to the proposed amendments? Please note that the Board will conduct Codification improvement projects on a periodic basis, and additional changes may be postponed to a subsequent Codification improvement project.

Response

See suggestions in the response to Question 1.

Also, to the extent that the Board is considering other amendments to ASC 820 as part of this project or otherwise, we think it is critical to coordinate such activities with the IASB to mitigate the risk of divergence or different interpretations in practice of ASC 820 and IFRS 13.

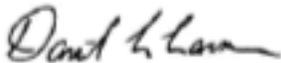
Question 4

The proposed amendments would apply to public and nonpublic entities. Would any of the proposed amendments require special consideration for nonpublic entities? If so, which proposed amendment(s) would require special consideration and why?

Response

We believe that any amendments pursuant to Issue 14 should have equal applicability to public and nonpublic entities.

We would be pleased to further discuss our comments with the FASB staff. Please direct any questions to either of us via the contact information set forth below.



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