December 9, 2019

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

Re: FASB Agenda Request – Fair Value Accounting Methodology

Dear Mr. Kuhaneck:

I respectfully submit the following request to the Financial Accounting Standards Board (FASB) to consider extending the use of fair value accounting beyond the currently acceptable accounting topics. Given that the topic can be a controversial one, I am requesting that the FASB consider adding a project to the Board's or Emerging Issues Task Force's agenda to address the potential expansion of fair value accounting and related disclosures.

Background

I appreciate the efforts of the Board and its staff in preparing ASC 820, *Fair Value Measurements and Disclosures*, and ASU 2011-04, *Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements*, which together define fair value and unify approximately sixty other accounting pronouncements that use the term. Specifically, ASC 820 provides a definition of fair value as "the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date". It also establishes a framework for measuring fair value and a hierarchy of inputs used to estimate it. What the topic does not do, is establish any new standards for *when* fair value measurement is required or permitted. Under U.S. GAAP, items currently reported at fair value consist of a small portion of the financial statements. Some examples of the use of fair value measurement in reporting are asset retirement obligations, derivatives and intangible assets acquired in a business combination. Other items are required to be reported using other methods, for example, property, plant and equipment must be measured at historical cost and depreciated over its useful life.

The Challenge

The use of fair value measurement requires a great deal of judgement. It also relies heavily on the market, which at times can be volatile and unstable. This can create challenges for preparers of financial statements. However, the argument that it is too challenging may not be a suitable argument in the future. Fair value measurement is gaining more favor in the eyes of the users of financial statements as it represents a more accurate picture of the company's assets and liabilities. As it is, many analysts have to utilize other financial information in determining their recommendations and very little users can rely solely on the financial reports to give valuable information. This seems inconsistent with the true purpose of financial reporting. The Securities and Exchange Commission (SEC) explains that financial statements taken together, “provide very powerful information for investors. And information is the investor’s best tool when it comes to investing wisely” (Beginners' Guide to Financial Statement, SEC). If the financial statements’ purpose is to provide powerful information to investors but it is hindered by conservative measurement approaches like historical cost, is it really providing the information that investors need? In reality, financial statement users are not interested in the cost of an asset but rather the benefits that asset is expected to provide over its life. In order to analyze a company’s position, users have to engage in a significant amount of research over and beyond the financial statement. This appears proof that the financial statements are not as powerfully informative as the SEC describes.

Another challenge in using fair value measurement is comparability. The methodologies used in determining an assets fair value differ significantly between preparers and can create inconsistencies in reporting. This is a challenge that has remained an obstacle for expanding the use of fair value. This is the reason FASB should add this matter to its agenda and create a project to streamline the fair value measurement methodologies. For example, the FASB could require that preparers disclose their process for “monitoring developments in valuation techniques to ensure that its valuation models appropriately reflect the types of inputs that market participants consider” (Fair Value Measurement, KPMG). This creates an obligation for preparers to defend their fair value methodology chosen in light of market participants’ perspectives (i.e. the purpose of financial reporting).

The Advantages

The most significant advantage of fair value measurement is its accuracy in terms of valuation. When an asset or liability’s value changes, the value reported to users also changes. It seems intuitive that the true value of an asset or liability be marked up or down to properly reflect what the company would receive or be obligated to pay if the asset was sold or the liability eliminated. With this methodology, investors are always kept informed on the true, real value of the company. This argument builds off of the conceptual framework, namely that financial information needs to be relevant. Furthermore, the use of fair value measurement requires that preparers disclose the changes made in the financials. This requires that preparers evaluate often their choices and can motivate better future decisions and thus improve business operations.

Another advantage to fair value measurement is the elimination of managing earnings by using gains and losses on sales of assets. Currently, managers can “arrange certain asset sales, to use gains or losses from the sales to increase or decrease net income as its desired time” (Advantages or Disadvantages of Fair Value Accounting, Jay Way). Contrarily, if using fair value measurement, the changes in value (i.e. gains and losses) would occur in the period in which the market experienced change (i.e. not when management deems desirable).

Conclusion / Recommendations

Based on the overall advantages of fair value accounting, I recommend the FASB consider expanding its use in financial reporting. Providing a more accurate, relevant picture of a company’s financial position is powerful information that users of financial statements need to make decisions. I think the primary purpose of financial reporting is to assist in making the market more efficient and therefore, a market value would more useful then historical cost.

Sincerely,
Candice Margiotta

References

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https://assets.kpmg/content/dam/kpmg/xx/pdf/2017/12/fair-value-qa-2017.pdf

3. Beginner's Guide to Financial Statement, SEC, 2007
https://www.sec.gov/reportspubs/investor-publications/investorpubsbegfinstmtguidehtm.html