



August 14, 2006

**Mr. Lawrence W. Smith**  
**Director – Technical Application and Implementation Activities**  
**Financial Accounting Standards Board**  
**Norwalk, Connecticut**

E-mail = [commentletters@pcfr.org](mailto:commentletters@pcfr.org)

File Reference = 1310-100

Dear Mr. Smith:

At the outset, please know how much we appreciate the efforts of both the FASB and the AICPA in developing the Invitation to Comment, entitled *Enhancing the Financial Accounting and Reporting Standard-Setting Process for Private Companies*. In our opinion, if the proposed framework is adopted for use by the FASB in the accounting standard-setting process, we believe that the end result will be that private companies will have financial reporting guidance that will result in more useful [relevant] financial statements that are more cost-beneficial to prepare. Formalizing the process of incorporating elements of differentiation into the standards for private companies [in certain circumstances] could only result in higher-quality financial statements for entities that are considered to be private [versus public] companies. So, for the work that has been accomplished to date, thank you.

We believe that the FASB should be applauded for its work in developing accounting guidance that is useful in addressing cross-border financial reporting issues, and we recognize the importance of the work that has resulted in new accounting standards that are helpful in addressing many complex reporting issues encountered by larger companies. However, within the context of financial reporting by private companies, some of the new [along with some of the old] financial reporting requirements result in financial statements that are not as useful for external stakeholders and too time-consuming [costly] for reporting entities to prepare.

**While there is little question that “complex” issues often need to be addressed with some “complexity” in the accounting guidance, some of the requirements associated with preparing financial statements using generally accepted accounting principles [GAAP] have just become too burdensome for many private companies so that many are choosing to “convert” GAAP-based financial statements to financial statements that are prepared using an other comprehensive basis of accounting [OCBOA]. And, in those circumstances where GAAP-based financial statements are prepared [and reported on], it is not uncommon for audit, review, and compilation reports to be modified because of GAAP departures in the financial statements. We believe that “driving” reporting entities to using bases of accounting other than GAAP and having CPAs/CPA firms modify reports on financial statements because of GAAP departures just will have the effect of eroding the quality of financial reporting by private companies.**

**Our responses to the questions where the FASB and the AICPA are requesting feedback on the Invitation to Comment are included in this overall response below. In summary, we agree with the FASB and the AICPA related to the importance of this project, and we are very hopeful that the decision will be made to implement the proposed guidance that should be helpful in developing high-quality accounting standards for use by private companies in accomplishing their financial reporting objectives.**

***Do you believe the proposal contained in paragraphs 16-29 will improve the accounting standard-setting process for private companies?***

**We are in total agreement with the FASB and the AICPA that there is a need to formalize the process related to considering the specific needs of private companies in developing accounting standards that must be utilized in GAAP-based financial statements. It is important to recognize that many private companies are “smaller” private companies where financial statements are being prepared [and reported on] to comply with financial reporting needs where end-users of the financial statements have access to management [owners] so that some of the requirements that typically are associated with general-purpose financial statements just might not be preferable for use in financial statements of private companies. Even in those cases where the end-users do not have access to management [owners] of private companies, some elements of differentiation would be helpful in the accounting standards through recognition of the fact that the financial reporting needs of private companies and users of financial statements of private companies simply differ from the financial reporting needs of public companies and users of public company reports. These differing needs should allow for some differentiation within the accounting guidance that should be used in developing the financial statements.**

**As just one example [among many] that could be used to illustrate the need for differentiation [the example is in the Invitation to Comment], while the provisions associated with SFAS No. 123R [share-based payments] should be helpful in financial reporting for public companies, since the FASB has eliminated the use of the “minimum value method” that existed in the “original” SFAS No. 123, private companies now need to devote a significant amount of time in determining fair value amounts [the “calculated value method”] where end-users of financial statements probably would have all of the information necessary for decision-making by allowing the continued use of the “intrinsic value method” [APB Opinion No. 25] that previously has been utilized for recognition/measurement. Feedback received through the AICPA Private Company Financial Reporting Task Force indicated that this is one of the elements of differentiation where end-users did not deem the “new” reporting model to be preferable to the “old” reporting model. Even with the lack of preferability, reporting entities need to incur a significant amount of incremental cost to comply with the SFAS No. 123R requirements even for “plain-vanilla” share-based arrangements.**

***Specific to paragraphs 16-29, do you believe that the proposed changes will help ensure that the financial reporting needs of constituents of private companies are met?***

**We are in total agreement with the FASB and the AICPA that the proposed changes should have the result of enhancing the input of private company financial reporting constituents to the accounting standard-setting process. As is too often the case today, the impact on private companies of newly-developed accounting standards might not be apparent to constituents of private company reporting until after-the-fact. The new model should help to ensure that the specific needs of private companies are considered in advance of accounting standards being finalized.**

**As just one example [among many] that could be used to illustrate this point, the FASB ultimately decided to defer [indefinitely] the effective date of SFAS No. 150 [mandatorily-redeemable equity] in financial statements for private companies where that document already had the result of requiring reporting entities to incur costs associated with rewriting equity agreements in advance of the FASB deferral of the requirements. Very commonly, private companies [for a variety of legitimate reasons] have equity instruments that are subject to mandatory redemption based on a single component [e.g., the death of the owner]. If the provisions within SFAS No. 150 had been required to be implemented, the end result would have been a “torpedo” to the equity section of balance sheets for many entities.**

**In some cases, the financial statements that would have been prepared [and reported on] for limited purposes [e.g., renewal of contractor licenses, etc.] for private companies, eliminating equity amounts would have had the catastrophic result of not allowing reporting entities to comply with minimum equity requirements and where the end-users of the financial statements would be “just as informed” with the disclosure of mandatory redemption requirements. The deferral of the effective date of that guidance is appreciated but it would have been better if the guidance never had been finalized so that reporting entities would not have incurred costs in anticipation of the guidance becoming final.**

**If the proposed approach to standard-setting had been in play with the development of certain accounting and reporting technical literature [e.g., SFAS No. 150], it is very likely that some of the unanticipated effects on financial statements of private companies would have been anticipated in advance of finalizing the literature. Recognizing these type facts/circumstances [financial statement effects] in advance of finalizing authoritative guidance should have the result of not having to “change the guidance” shortly after “finalizing the guidance” so that reporting entities do not have to incur unnecessary costs in order to avoid unintended consequences associated with the accounting technical literature.**

***The FASB and the AICPA believe that any differences in generally accepted accounting principles [GAAP] for private companies should be based on financial statement user needs and cost-benefit considerations. Do you agree?***

**We are in total agreement with the FASB and the AICPA that any elements of differentiation within the accounting standards for private companies should be considered using the user-needs and cost-benefit criteria. In those circumstances where end-users would be better served by having financial statements that are “different” [in certain circumstances], and/or in those circumstances where the end-users do not care about information that would be in financial statements as a result of implementing new technical literature [the user-needs criterion], then it is difficult to argue that reporting entities should incur the cost to comply with the technical literature requirements [the cost-benefit criterion]. While operationalizing these two criteria might be somewhat difficult, we agree that these two criteria should be utilized in making decisions related to whether it is preferable to have elements of differentiation within the accounting standards for private [versus public] companies.**

***The FASB and the AICPA believe that members of the committee [except the chair] should not be compensated beyond a reasonable reimbursement of expenses. Do you agree?***

**This question might be the most difficult question where the FASB and the AICPA have requested feedback. Since the work of the newly-created [as proposed] committee will/should have such a significant impact on financial reporting by private companies, it will be important to have the “right people” involved in this work. Forming a committee where members just “have the time” [rather than members who will “prioritize the time”] to do the work might have the result of having a committee that is not effective in accomplishing committee objectives.**

**One of the greater challenges in getting the “right people” to be involved in this work probably will be attracting the “right people” from the external stakeholder group and from within reporting entities where the time might not be available to prioritize for this important work. Historically, one of the challenges of getting input from CPAs in public practice in “smaller” practice units has been just the lack of time [because of client responsibilities] to get involved in the process; the same type challenge exists when trying to attract the “right people” from the external stakeholder group and from within private companies. However, we tend to agree that committee members [other than the chair] should not be compensated because there should be enough of the “right people” to volunteer time for this important endeavor without having to incur another “layer of costs” related to the standard-setting process. Providing compensation for service still would not alleviate the demands on the time of the “right people” with responsibilities where time simply does not exist because of those responsibilities. Essentially, if the time does not exist, then trying to pay for that time would be unworkable. So, while we certainly can understand [and appreciate] a position to the contrary, we agree that the committee members [other than the chair] should not be compensated for service on this newly-created [as proposed] committee.**

***The FASB and the AICPA believe the committee should set its own agenda and priorities. Do you agree?***

**We are in total agreement with the FASB and the AICPA that the newly-created [as proposed] committee should have the ability to set its own agenda. While the agenda will need to be influenced by the FASB agenda, the particular issues that need to be addressed should be developed within the committee.**

**We appreciate the opportunity to provide feedback on the Invitation to Comment. And, we look forward to “continuing progress” by the FASB and the AICPA related to this important work.**

***Thomas A. Ratcliffe***  
**Director, Accounting & Auditing**