

October 3, 2007

Ms. Nancy M. Morris
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: File Number: 265-24 – Discussion Paper for Consideration by the SEC Advisory Committee on Improvements to Financial Reporting (Discussion Paper)

Dear Ms. Morris:

The Financial Reporting Committee ("the FRC") of the Institute of Management Accountants ("IMA") appreciates the opportunity to provide its views on the "*Discussion Paper for Consideration by the SEC Advisory Committee on Improvements to Financial Reporting*" (the "Discussion Paper"). The FRC is the financial reporting technical committee of the Institute of Management Accountants. The FRC is comprised of representatives from preparers of financial statements from some of the largest companies in the world, the largest accounting firms in the world, valuation experts, accounting consultants as well as academics. The FRC reviews and responds to research studies, statements, pronouncements, pending legislation, proposals and other documents issued by domestic and international agencies and organizations.

As a starting point we commend the Securities and Exchange Commission ("SEC") for under taking this important initiative. In addition, we agree and support the *SEC advisory Committee on Improvements to Financial Reporting's* (the "Committee") mandate of

looking for ways to reduce unnecessary financial reporting complexity and making information more useful and understandable for investors.

We have reviewed the Discussion Paper and agree with the basic approach being adopted by the Committee in that the Committee is focusing on the major areas and we like the idea of identifying within one year, a few ideas that can be made operational. Additionally, we believe the major topics being addressed by the various sub-committees appear appropriate. We have limited our comments in this letter to topics where the FRC has the most expertise, namely financial reporting complexity and the accounting standard setting process. Specifically, in the balance of this letter we describe what the FRC views as some of the underlying causes of financial reporting complexity (including the role of the accounting standard setters in financial reporting complexity) and some preliminary thoughts on what can be done to reduce financial reporting complexity. Going forward we will closely monitor the progress of the Committee's work and may have additional comments and observation which we may wish to share with you as well.

Causes of Financial Reporting Complexity

In attempting to discern some of the causes of financial reporting complexity we believe the Committee may hear different perspective from different constituencies. In particular, we have found that each of the stakeholders in the financial reporting process views the issues in this area in terms of what they observe directly through the roles they play. Our sense of the perspectives of financial statement preparers, auditors and users of financial statements as it relates to the causes of financial reporting complexity is set forth below.

1. **Financial Statement Preparers.** Preparers of financial statements believe that financial reporting complexity results from:

- An unforgiving regulatory and legal environment that makes a financial statement preparer reluctant to exercise good faith professional judgment;

- Operational complexity as a result of complex standards or accounting terms that are difficult to apply (i.e. how should one calculate expected losses in accordance with FIN 46 *Consolidation of Variable Interest Entities*).
- Standards wherein the resulting accounting is inconsistent with management's views of the underlying economics of a transaction. For example, under an FASB accounting standard on accounting for non-controlling interests (which is close to being finalized) a company would be required to record gains or losses upon purchasing a controlling interest in a business for which it previously held a minority interest. It seems unusual to record a gain or loss upon consummation of a purchase transaction for a business the company continues to own.
- The sheer volume of guidance in standards and the proliferation of interpretations from multiple sources (FASB Staff, SEC Staff, Accounting firms) and in many forms (formal rules, informal interpretations, speeches). Additionally, certain of the accounting standards have become so complex that they can only be understood by a relatively small group of experts residing in the National Office of major accounting firms.
- The existence of standards based on inconsistent concepts and principles.

More specifically, we believe complexity is caused by some of the following factors:

- The current legal and regulatory environment creates complexity due to the financial and reputational risks that exist, even when good-faith efforts are made to comply with the rules. We believe that complexity can be mitigated by having principle based standards but only if there is a change in the current regulatory environment (such changes are discussed later in this letter).
- On occasion companies are asked to restate their financial statements for matters in which there is no clear accounting rules but because someone on the SEC staff would have reached a different judgment. Such actions result in the development of informal interpretations of accounting requirements that are not widely understood by financial statement preparers and undermine confidence in financial reporting.

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Moreover, such actions result in preparers wanting detailed accounting guidance on fairly narrow scope issues which exacerbates financial reporting complexity.

- The lack of a fully developed conceptual framework leads to inconsistent concepts and principles being applied across accounting standards. For example, the accounting model for recording non-tax contingencies is based on a probable loss notion while tax contingencies are based on a more-likely-than-not notion and guarantees of a contingency are recorded at fair value. And in a business combination, the accounting for contingencies will be different under the new FASB 141(R).
- The accounting standards have different measurement attributes (such as historical cost or fair value) and different accounting treatment alternatives (an investment in an equity security can be marked to fair value in the statement of operations or in the statement of shareholders equity). Many attribute financial statement preparers' reluctance to accept fair value accounting to an aversion to volatility. In our view, while we agree that companies are somewhat concerned over the earnings volatility impact(s) of utilizing fair value measurement attributes, they are more concerned over the relevance and reliability of measuring non-financial assets and liabilities at fair value when those assets and liabilities do not have readily available markets to determine fair value.
- Many view exceptions to standards as contributing to complexity. We do not believe that an exception included in a standard, necessarily increases complexity and at times such exceptions actually reduce complexity. For example, a simple purchase order to buy a fungible product for use in a business would have been considered a derivative instrument under FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities* ("FAS 133"). An exception in FAS 133 provided that such contracts were scoped out from such accounting. This is an example where the standard needed to be "scoped back" to avoid an accounting treatment that would be completely inconsistent with the underlying economics and operational aspects of a particular transaction.

