

July 13, 2011

Board of Trustees
Financial Accounting Foundation
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Board Members:

The purpose of this letter is to communicate our Firm's views regarding the future of financial accounting standard setting for private companies and not-for-profit organizations.

BerryDunn is a regional firm that audits approximately 500 private companies and not-for-profit organizations. We also audit a small number of SEC registrants.

It is our belief that the debate over "public company" vs. "private company" GAAP has a misplaced focus, as it is centered on the nature of the entity issuing financial statements. We believe the focus should instead be on the needs of users of the financial statements.

As GAAP has evolved, and especially in the past 10-15 years, we have observed increased disparity in the needs of users of financial statements. These needs tend to relate to one of two perspectives:

1. A combination fair value/cash flow (often referred to as "mixed attribute") perspective, which tends to be the primary focus of users of SEC registrant financial statements (and perhaps some companies whose securities are traded locally). These users are interested in information that helps them determine a company's fair value, thereby enabling investment decisions. This information includes both fair value information regarding certain assets and liabilities, as well as historical cash flow data that may be used (with appropriate adjustments) to forecast future cash flows, typically the key determinant of an entity's fair value. As these users buy and sell relatively small interests in the companies they invest in, they typically do not have access to information beyond that which is publicly available, including the companies' financial statements and related information filed with the SEC. It is our view that GAAP as currently promulgated appears to have this perspective as its objective.
2. A cash flow perspective, which tends to be the primary focus of users of financial statements of privately held companies and not-for-profit organizations. These users are interested in information that helps them determine an entity's use of resources they provide, and ability to repay those resources when required. Users with this perspective include lenders to for-profit and not-for-profit entities; and donors, grantors and other providers of resources to not-for-profit organizations.

A number of new accounting principles promulgated in the last 10-15 years have increased GAAP's focus on fair value measurements. Examples include accounting for derivatives and other financial instruments, share-based payment, and goodwill. These pronouncements arguably enhance the value of information provided to users in the first category above, as they provide management's perspective on values of components of the enterprise. They often, however, bear little direct correlation to current

or reasonably foreseeable cash flows of the entity, and thus are perceived as of little value to the second group of users described above. In our experience, such users often adjust the reported financial information to “factor out” such fair value-based information, in order to better understand and assess entity cash flows.

There are certainly times when fair value-based information is valuable to users of private company financial statements. A common example is a potential investor in, or purchaser of, such an entity. In our experience, however, such a user is typically in a position to request additional information of the entity’s management (such as budgets, planned management changes, and other information that may be more useful in assessing fair value than historical financial information), and rarely makes such a decision based solely on the entity’s GAAP financial statements.

Instead of mandating a particular set of financial accounting rules based on the characteristics of an entity (i.e., as a “public” or “private” company), we recommend two bases of accounting be developed, which are responsive to the two groups of users described above. Currently, subject to the needs of users, entities have the option of preparing financial statements based on GAAP, or on an other comprehensive basis of accounting (OCBOA) such as the cash basis, income tax basis, and so forth. We propose that this ability to tailor financial information to meet the needs of users be enhanced by development of two formally promulgated bases of accounting, as follows:

1. A “mixed attribute” basis, which seeks to provide information to users relating to both fair value of individual assets and liabilities and historical cash flows, to assist them in assessing the fair value of an entity. This basis would make use of many elements of current GAAP that focus on fair value, such as accounting for derivatives, stock options, and annual impairment assessments of goodwill. We believe it would be important to present financial information under this basis in a manner that enables users to distinguish cash flows from other items reported in the financial statements, as historical cash flows are often important in the assessment of fair value.
2. A “cash flow” basis, which seeks to provide information to users to assist them in assessing an entity’s use of resources, and ability to repay them when required. Many of the current “noncash” accounting requirements that have been the subject of criticism by these users, or are “factored out” by them when they analyze entity financial statements, would not be applicable to this basis of accounting, thus enhancing the usefulness of the financial statements to these users. It would still be appropriate to recognize impairment losses in certain circumstances; such losses would represent a “reclassification” of historical cash flows from asset to loss, when it is considered probable amounts recognized as assets do not reflect ability to generate future cash flows from such assets.

As with the various OCBOAs, a given entity would then have the ability to choose which basis of accounting better meets the needs of its users. The SEC would presumably require the “mixed attribute” basis (and rightly so), while most private companies and not-for-profit organizations would likely conclude the “cash flow” basis better meets the needs of the primary users of their financial statements. A private company that plans to seek investors, for example, through a public offering or private placement, may elect to present its financial statements using the “mixed attribute” basis, as it anticipates a new set of users with different needs.

Should the Financial Accounting Foundation (FAF) move forward with such a methodology, we believe the requirements under both bases of accounting described above should be promulgated by a single standard setter, such as the Financial Accounting Standards Board (FASB). As a firm that performs

audits under both American Institute of Certified Public Accountants and Public Company Accounting Oversight Board standards, we have seen the unnecessary and, at times, unintended complexity that can arise from having two standard setters prescribe audit rules for similar situations, and we believe the likelihood of such complexity, and the attendant cost and waste of preparer and auditor resources, would be exponentially greater in the arena of accounting standards. A single standard setter, such as FASB, could address a given issue by considering how best to provide information to both sets of users described above; such an exercise could add clarity to its analysis, and ultimately result in better standard setting under both bases of accounting.

While our proposal does not specifically address international accounting standards, we have seen the International Accounting Standards Board (IASB) wrestle with the same issue, thus resulting in the promulgation of “full international financial reporting standards (IFRS)” and “IFRS for small and medium-sized entities (SMEs).” While this dichotomy was the IASB’s attempt to address the public vs. private company issue, it is again focused on the characteristics of the reporting entity rather than the needs of its users. As a result, IFRS for SMEs lacks a conceptual framework, and is likely to be maintained and updated going forward on the basis of difficulty of implementation of rules, rather than value provided to users. Accordingly, the FAF and FASB have an opportunity to exercise global leadership by putting forth a user-needs based model, which the IASB may find valuable as it strives to address the same problem in an effective manner.

We appreciate the opportunity to submit these observations for your consideration, and look forward to the Foundation’s continued proceedings in this important area.

Sincerely,

A handwritten signature in cursive script that reads "BerryDunn".

BERRYDUNN