




**National Rural Electric  
Cooperative Association**

A Touchstone Energy® Cooperative 

**Via Email**

August 8, 2008

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

Re: File Reference 1600-100

Dear Sir or Madam:

The National Rural Electric Cooperative Association (“NRECA”) is the not-for-profit national service organization representing approximately 930 not-for-profit, member- owned rural electric cooperatives. The great majority of these cooperatives are tax-exempt distribution cooperatives that provide retail electric service to over 40 million consumer- owners in 47 states. NRECA members also include 65 generation and transmission cooperatives that supply wholesale electric power to their distribution cooperative member-owners.

On behalf of our membership, we are responding to the request for comments to the Exposure Draft document *Disclosure of Certain Loss Contingencies* which was released on June 5, 2008.

***Enhanced disclosures of certain loss contingencies may be intended to provide useful information to assist users of financial statements in assessing the likelihood, timing and amount of future cash flows – but at a substantial direct and indirect cost to the companies we represent.***

## **TRANSPARENCY**

The paradox of increased transparency concerns us. If one defines transparency as providing users of financial statements access to a broad range of information without filtering by the entity, then we feel that the corollary from the financial statement user’s point of view must also be considered. That is, increased transparency places a responsibility on the user of financial statement information to make a self determination as to the information’s relevance, probability and quantitative impact upon cash flows. When making this determination, different users may come to equally valid, but differing conclusions. The collective process of many users making such determinations is, by definition, imperfect; not only due to perceptual and cognitive differences regarding the information itself, but also users may be unconsciously biased by the manner in which the information is presented by the entity.

### **Interpretation of data**

A case in point is the wide range of disclosures surrounding the application of Financial Interpretation (FIN) No. 48. While the criteria of FIN 48 appeared straightforward, the tremendous divergence of disclosures in practice illustrates our concern. If the Exposure Draft is adopted as proposed, entities will have widely divergent disclosures, as was the case when FIN 48 was adopted. We believe that the likely outcome will be that comparability of information between entities will be compromised as a result of the potential wide range associated with how entities describe the disclosures of certain loss contingencies in their financial statements.

We also believe there is a wide gulf between the disclosure of a loss contingency and the ability of a user of the financial statements to assess the potential impact of such an event on future cash flows of the enterprise.

### **LEGAL IMPACT**

It is quite likely that enterprises will incur additional legal costs, perhaps substantial legal costs in walking the fine line between responsive disclosure and revealing too much information to the plaintiff's bar. We concur with the observations of the Financial Accounting Standards Advisory Council that the Exposure Draft has the potential to increase litigation.

We believe the FASB should narrow the disclosures related to pending or threatened litigation. Possible losses related to actual or potential litigation are often difficult to quantify since courts have wide latitude to consider not only the precedent of prior case law, but to interpret the facts and circumstances before the court.

In this regard, it will ultimately be a legal determination as to whether the potential of loss related to possible claim or assessment is remote. ***We STRONGLY believe that the concept of remote is perhaps too restrictive in matters involving potential claimants and would suggest that in matters involving actual or potential litigation a more useful standard would be likely or reasonably probable—that is, a concept with a broader threshold than remote.***

### **AUDIT ISSUES**

We are concerned that the Exposure Draft may require the American Bar Association to reconsider the content of the standard legal letter for a financial statement audit. Given the proposed effective date of the potential new standard, we are not certain that any such amendments in the legal letter, if required, could be accomplished within the time frame for the preparation of the audits of entities with calendar year ends. Since the determination of the content of the audit legal letter has been a joint collaborative process in the past with the auditing profession, we respectfully suggest that the FASB consider this potential implication when considering the final effective date of any new standard.

### **QUALITATIVE AND QUANTITATIVE INFORMATION REGARDING LOSS CONTINGENCIES**

We believe that users of financial statements will need qualitative information in order to assess the potential impact upon future cash flows of the entity. However, we do not feel that entities will in practice provide information that will ultimately enable a broad range of financial statement users to achieve their goals in this regard. Quantitative information in this area is notoriously subjective and

perhaps the FASB could consider a disclosure requirement cautioning the reader of the financial statements of this fact. With this in mind, we feel that information regarding a potential range of loss is more useful than the illusion of a specific number which may give the chimera of precision when, in fact, no such certainty exists.

#### **DISCLOSURE OF SETTLEMENT OFFERS SHOULD NOT BE REQUIRED**

Settlement offers of counterparties in disputes are often ephemeral and fleeting. We do not believe that such disclosures would provide useful information since any such disclosure would have to be accompanied with such qualifying language as to make it essentially meaningless in all but the most robust of circumstances.

#### **TABULAR DISCLOSURE OF AGGREGATE LOSS CONTINGENCIES IS USEFUL INFORMATION IN ASSESSING FUTURE CASH FLOWS**

The focus of the Exposure Draft is on the assessment of future cash flows; we believe this can best be achieved by the utilization of aggregate loss contingencies rather than potential losses quantified on a singular basis. Tabular disclosure will aid users of financial statements in assessing the changes in such information between reporting periods and this should enable users to better assess the reliability of such disclosures by the entity over time.

As we have seen with the disclosures concerning FIN 48, the information provided by certain entities will undoubtedly be perceived to be more reliable from the point of view of a user of the financial statements. This is an inevitable outcome when disclosures are inherently subjective but is not a reason, in our view, to eliminate the aggregate disclosure of quantitative information.

#### **DISCLOSURES REGARDING PREJUDICIAL INFORMATION**

We concur with the FASB's proposal to aggregate potential prejudicial information or, in the case of a single legal dispute, to forgo disclosing information that would be prejudicial to the entity's position. We believe that such a qualification will strike a reasonable balance between the need of financial statement users for transparent information and the need of the entity to avoid disclosures in which counterparties could glean useful information in the pursuit of their claim.

#### **DISCLOSURE OF A MAXIMUM POSSIBLE LOSS IN CASES WHERE THERE IS NO CLAIM OR ASSESSMENT MAY BE PREJUDICIAL IN A BROAD SENSE**

We strongly believe that the requirement to disclose a maximum exposure of loss in the event of claim or assessment is prejudicial. That is, the disclosure of such information could affect, to the detriment of the entity, an outcome of the contingency itself.

It seems to us, however, that the concept of prejudicial may actually be broader than described above in the sense that such disclosures may entice the plaintiff bar to pursue litigation after reading the financial statement disclosures of an entity applying the language in the Exposure Draft, should it become a final statement. Alternatively, the financial statements of the entity could be introduced as evidence and used against the entity in a court of law. If this were to happen, disclosures of loss contingencies in such situations may become a self-fulfilling prophecy, and one could assert that the disclosure affected the

entity in a detrimental manner. We do believe that users of financial statements will find such disclosures generally useful, **but we do not see an escape from this potential paradox of disclosure and prejudice.**

#### **INTERNATIONAL ACCOUNTING STANDARDS (IAS) 37 PROVISIONS, CONTINGENT LIABILITIES AND CONTINGENT ASSETS**

The International Accounting Standards Board (IASB), is currently considering amendments to IAS 37. Specifically, paragraph 92 of IAS 37 currently indicates that circumstances in which the prejudicial exemption would be utilized to be *extremely rare*.

We concur with the majority view of the FASB that the term *extremely rare* would be difficult to apply in practice and we encourage the FASB, should a final standard in this area create a convergence opportunity with the IASB, to be resolute in the use of the word *rare* as opposed to the current IAS 37 qualifier.

#### **PRACTICAL CONSIDERATIONS REGARDING THE PROPOSED EFFECTIVE DATE**

Considering the relatively short time that entities would have to read , understand, and implement a final standard for calendar year 2008, not to mention the time it would take the entity's counsel to do the same, we feel that the proposed implementation date is somewhat aggressive. Even if the FASB were to issue a final standard by the end of the third quarter, preparers of financial statements would only have a matter of a few months to implement the new standard for the first time. We believe that a new standard on loss contingencies, since it is somewhat the antithesis of SFAS 5, may require longer lead time to merge into the financial statement reporting process and we encourage the FASB to consider and balance the needs of users and preparers of financial statements when determining a final effective date.

#### **CONCLUSION**

We appreciate the opportunity to comment on the Exposure Draft and we look forward to working with the FASB staff on this project as it unfolds in the coming months. Any new financial accounting standard is a balancing act between the needs of users and preparers of financial statements and the Exposure Draft is the quintessential illustration of that maxim. We believe that users of this information will be undertaking a burden when trying to apply what we expect to be a widely diverse range of disclosures regarding loss contingencies. Concurrently, the preparers of the financial disclosures will likely be faced with increased cost, increased litigation or threat thereof and, wide variance of interpretation of application.

If you have any questions, or if I may be of assistance in any capacity, please do not hesitate to call upon me.

Kind regards,

/s/Russell D. Wasson  
Director, Tax, Finance and Accounting Policy

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