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Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549

RE: Fair Value “Accounting” and the Emergency Economic Stabilization Act of 2008

Sir/Madam:

There are, at a minimum, 700 billion reasons why fair market valuation, as promulgated by the Financial Accounting Standards Board and espoused by Wall Street economists, has become a topic of animated, if not contentious, discussion.

On the morning of December 1, 2008, WCBS Radio (New York) commented on current consumerism’s appropriately shifting to a reliance on salaries and savings rather than on “**false** values invented out of thin air by [financial institutions].”

We—the FASB, the SEC, CPAs in practice—understand and accept accountability. Accountability leads us to recognize that we have played some part in the current global economic crisis—in the deluge of inflated economic valuations, unsustainable asset appreciations, and irresponsible credit expansion. But our accountability also gives us an opportunity to correct, to reverse, certain of the excesses that helped to create this current crisis.

Our accountability demands that we give careful, skeptical consideration to the adoption of the economic theory of fair market valuation. Some thoughts follow:

SUMMARY RECOMMENDATION

The SEC has promulgated Regulation S-X and S-K to provide financial statement disclosure and disclosure of other financial data. To date, the SEC has been quite clear that forward-looking statements—projections and other information of a speculative nature—are properly presented in S-K disclosures¹, not in S-X disclosures.

The Accounting profession should support—not oppose—these long-standing SEC directives. Marking non-marketable assets to market and other such speculative applications of fair market valuation theory, as promulgated by the Financial Accounting Standards Board, while providing relevant data to certain segments of the investing community, should be identified as “projected/forward-looking” disclosures and, therefore, presented under Regulation S-K. To present other than as S-K invites

¹ Regulation S-K provides for and encourages forward-looking information in Management’s Discussion and Analysis in Form 10-K. The SEC’s safe-harbor rule (Rule 3b-6 under the Exchange Act and Rule 175 under the Securities Act) provides a defense for inaccurate forward-looking data, as long as management had a reasonable basis for the information and issued the information in good faith. Therefore, projections and speculative fair-market valuations, based on the SEC’s encouragement and safe-harbor provisions for forward-looking information, would properly be presented as Regulation S-K disclosures, not S-X.

misinterpretations and misunderstanding of the level of risk inherent in projections and fair market valuations and consequent misplaced reliance on same financial data.

The reporting guidelines of Regulation S-X should not be confused or merged with the guidelines of Regulation S-K. There is value to both historical costing and to fair market valuation. Both should be presented—in appropriate fashion, under the appropriate SEC Regulation. Complying with SEC Regulations serves the entire public.

Relevance

Issue

The Accounting profession must provide financial data that users deem relevant—timely and predictive. Otherwise, the Accounting profession fails in its obligations to the public. A puzzle arises, however, as we define the “public” and its “needs.”

Financial data requested and used by Wall Street are frequently different from data sought by banking/lending institutions and by business managers. Yet all these groups, and more, are “the public.”

Recommendation

The Accounting profession should address the different financial needs of different members of the public with different financial disclosures.

Accountants should use both historical cost and fair market valuation, depending upon the financial instrument being disclosed and depending upon where the disclosure is to be made. (See “Financial Presentation” below.)

By presenting financial data that all users need, the Accounting profession can continue to provide data that are by definition “relevant” to all users.

Conservatism; Reliability; Comparability

Issue

Many in the Accounting profession have expressed concern that adoption of the FASB’s model of fair market valuation promotes “relevance” at the expense of accounting concepts and qualitative characteristics that have served the public well for generations.

Many accountants—indeed, investors—have requested a re-focus on . . .

- Conservatism—the constraint that, when in doubt, one must select the accounting alternative that would be least likely to overstate net income or net assets
- Reliability—the financial characteristic of being verifiable
- Comparability/Consistency

Recommendation

Financial data that are not reliable, comparable, and conservative, cannot be relevant. Accounting concepts/characteristics cannot be mutually exclusive.

To be relevant, fair market valuation must consider not merely a few accounting concepts, but rather all the concepts/characteristics. Fair market valuation that is not, for example, reliable has little use to an astute investor.

Accountants should tailor the application of historical cost and fair market valuation depending on the financial instrument being presented and where the disclosure is to be presented. (See “Financial Presentation” below.) The Accounting profession

must construct financial statement/data presentation that is rooted in all concepts and characteristics.

Financial Presentation

Issue

Where in financial statements should fair market valuation be applied? Can historical cost and fair value be presented compatibly, simultaneously, for the benefit of all users?

Recommendation

Fair market valuation of marketable assets should continue to be disclosed in SEC Regulation S-X financial statements. Examples of such assets include short-term investments and customer accounts receivable.

Speculative valuations attached to non-marketable financial instruments (such as, typically, fixed assets), forecasts, projections, and forward-looking disclosures should not be components of the balance sheet. These data are more properly represented in SEC Regulation S-K disclosure.² To accommodate enhanced fair market disclosure, Regulation S-K could be appended as needed.

There should be no argument that fair market valuation of non-marketable financial instruments is an economic exercise that has no rationale for accounting presentation in SEC Regulation S-X financial statements.

Going Concern Disclosure

Issue

The Accounting profession has noted that, in cases of an entity's likely demise, fair market valuations of assets and liabilities can be more relevant than historical costs. An extreme example of this is the financial position of an entity during bankruptcy proceedings:

- A liability of a bankrupt entity is not what had been originally agreed by the contracting parties, but is what is established via bankruptcy proceedings.
- The building and land the entity holds should not be valued at historical cost; rather, they are worth what the market/liquidator determines, since near-term liquidation is to be the ultimate disposition of these assets.

When, then, should fair market valuations supplant historical cost? Where should such disclosure be presented?

Recommendation

Because a financially robust entity has different financial reporting needs from those of a financially stressed entity, the Accounting profession should consider financial disclosures to reflect this. Additional financial disclosures should be adopted in the case of financially stressed entities.

At a minimum, the Accounting profession should consider a Regulation S-K disclosure in the case of a "going concern." Any entity with a "going concern" clause in the independent accountants' opinion should be required to present an additional fair

² As discussed in more detail above, Regulation S-K provides for projections and forward-looking information to be disclosed in Management's Discussion and Analysis in Form 10-K.

market balance sheet under Regulation S-K. This fair market balance sheet would present values at “exit prices”—the amounts that would be received when selling an asset or be paid when transferring a liability. Additional S-K disclosures might be warranted.

Therefore, a “going concern” entity would present its Regulation S-X balance sheet as required—necessary for the entity in its dealings with lending institutions, for example—and simultaneously would present “exit-priced,” fair market disclosures that are especially relevant during the “winding up” of an entity.

Fraud (?)

Issue

The FASB has promulgated the fair market concept that a liability should reflect its nonperformance risk (the risk that the liability/obligation will not be paid/met). The FASB has stressed that nonperformance risk must include an entity’s credit risk.

Application of this promulgation could result in an entity’s eliminating a liability from the balance sheet, not by actually fulfilling the obligation, but instead by merely positing the risk that the obligation shall not be met. This result has been labeled by many outside the FASB as counterintuitive, since the liability’s elimination because of credit risk results in a corresponding increase in income!

The FASB’s application of fair market valuation to liabilities, besides being counterintuitive, raises a number of serious questions:

- Should a valid liability, legally documented, verified, and admitted to exist by the party that owes the money, be permitted to be written off for no reason other than risk of default—“nonperformance risk”?
- Should the Accounting profession support the financial community so that lending institutions can continue to rely on a prospective borrower’s balance sheet to learn of the borrower’s total legal obligations/debts—no matter what the borrower’s risk of nonperformance might be?
- Should the Accounting profession promote financial statement presentation of:
(1) the debt/obligations that an entity is legally accountable to fulfill or, instead,
(2) the debt/obligations that an entity projects it will be able to fulfill?

Recommendation

Underreporting liabilities cannot be permitted, no matter what economic theory, fair market rationale, or spurious argument might be postulated. Until and unless both parties to a liability—the party that is to pay and the party that is to receive payment—agree to terms to reduce or eliminate a liability³, that liability must be presented on the balance sheet in its entirety. Anything less would not fairly present an entity’s financial position—and arguably must be judged to be fraudulent disclosure.

In addition, there is no disclosure that can adequately replace a valid liability that has been sponged from a balance sheet via fair market rationale. Good disclosure cannot cure bad accounting.

³ Note that a legal proceeding, such as a court order related to bankruptcy, can reduce an entity’s liability without any payment being made. In such a case, both parties to the liability do in fact agree to change the obligation, by reason of the binding legal ruling.

