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Chairman Robert H. Herz
Financial Accounting Standards Board
401 Merritt 7
Norwalk, Connecticut 06856-5116

Re.: Invitation to Comment – *“Enhancing the Financial Accounting and Reporting Standard-Setting Process for Private Companies”*

Dear Chairman Herz and Board Members:

I have been significantly engaged in both SEC and private company financial accounting and reporting my entire career that now exceeds 30 years.¹ I am the President of the Colorado State Board of Accountancy and serve as a member of the PCAOB Standing Advisory Group. I have the following comments regarding *Enhancing the Financial Accounting and Reporting Standard-Setting Process for Private Companies* (the “Proposal”).

The Proposal does not address the statutory authority required to create Private Company GAAP. Currently, that jurisdiction resides with State Boards of Accountancy. Absent the support of these state regulatory authorities the ability to promulgate Private Company GAAP will be tenuous at best.

Defining “Generally Accepted Accounting Principles” has evolved from loose interpretations to full regulatory status today for Public Company GAAP. On the other hand, Congress has never stipulated formulation of Private Company GAAP, leaving that decision to the States and market forces. This laissez faire approach has contributed to confusion about who has the right to set standards. Clearly, this chain of authority “missing link” needs to be resolved so as to lay a solid foundation for Private GAAP.

Until recently, this authority “linkage” was largely ignored or conveniently overlooked, but the Constitution reserves this power to State Boards of Accountancy, the duly appointed representatives of the “People:”

The powers not delegated to the United States by the Constitution, nor prohibited by it to the states, are reserved to the states respectively, or to the people.²

After the 1929 market crash, Congress charged the SEC “(t)o prescribe the methods to be followed in the preparation of [financial] reports.” Historically, the SEC has “looked to the private sector in establishing accounting principles.”³ This prescription expanded with passage of the Sarbanes-Oxley Act of 2002.

After passage of Sarbanes-Oxley, the FASB formally requested that the SEC recognize it as the “designated organization in the private sector for establishing standards of financial accounting and reporting.” The request was granted,⁴ but the SEC’s jurisdiction runs solely to public companies, so the question of Private Company GAAP was left unsettled. In the words of the Act itself (underlining added):

¹ I am Ehrhardt Keefe Steiner & Hottman’s Director of Accounting and Auditing Quality Assurance; I serve on the board of directors of NASBA and on an AICPA senior technical body, the Professional Ethics Executive Committee. As noted, I am President of the Colorado Board of Accountancy and a member of the PCAOB Standing Advisory Group. However, the views expressed herein are solely my own.

² U.S. Constitution, Article X

³ SEC Chairman William H. Donaldson quoted in *FASB: 30 Years of Setting the Standard*, The FASB Report, September 30, 2003

⁴ SEC Financial Reporting Release No. 1, Section 101; reaffirmed in a SEC April 2003 Policy Statement

CONSIDERATIONS BY APPROPRIATE STATE REGULATORY AUTHORITIES.

In supervising nonregistered public accounting firms and their associated persons, appropriate State regulatory authorities should make an independent determination of the proper standards applicable, particularly taking into consideration the size and nature of the business of the accounting firms they supervise and the size and nature of the business of the clients of those firms. The standards applied by the Board under this Act should not be presumed to be applicable for purposes of this section for small and medium sized nonregistered public accounting firms.⁵

The Act also defines “appropriate state regulatory authority”:

DEFINITIONS.

(a) IN GENERAL.—In this Act, the following definitions shall apply:

(1) APPROPRIATE STATE REGULATORY AUTHORITY.—The term “appropriate State regulatory authority” means the State agency or other authority responsible for the licensure or other regulation of the practice of accounting in the State or States having jurisdiction over a registered public accounting firm or associated person thereof, with respect to the matter in question.⁶

Given these legal underpinnings, the FASB should secure a “designation” from “appropriate state regulatory authorities,” in a similar manner as it did from the SEC. Recognizing the difficulty in dealing with 55 different jurisdictions, the logical course of action would be to open a dialogue to accomplish this with the State Boards through the National Association of State Boards of Accountancy.

Based on the foregoing:

- ◆ The foundation of the Private GAAP concept should be clarified by establishing the authority of the FASB as the “designated” private-sector standard-setting body.
- ◆ This “designation” should incorporate the participation of State Boards/NASBA in the Private GAAP deliberative process.
- ◆ The designated private-sector standard-setter should control the Private GAAP agenda. Arrangements to the contrary are not in the public interest.
- ◆ All advisory committee activities should be subject to the independent processes of the designated private-sector standard-setter and not “shared” with any other private interest group. Arrangements to the contrary are not in the public interest.
- ◆ Please consider the structure of the PCAOB Standing Advisory Group as an alternative model.⁷

Thank you for your consideration,



⁵ Sarbanes-Oxley Act of 2002, § 209

⁶ Ibid., § 2

⁷ PCOAB Release No. 2003-009, *Compliance with Auditing and Related Professional Practice Standards*, http://www.pcaobus.org/rules/docket_004/2003-06-30_release_2003-009.pdf