

January 7, 2004

Letter of Comment No: ⁶
File Reference: FSP8524A

Mr. Lawrence Smith
Director of Technical Application and Implementation Activities
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, Connecticut 06856-5116

Re: Proposed FASB Staff Position No. EITF 85-24a, *Application of EITF Issue No. 85-24 "Distribution Fees by Distributors of Mutual Funds That Do Not Have a Front-End Sales Charge," When Cash for the Right to Future Distribution Fees for Shares Previously Sold Is Received from Third Parties*

Dear Mr. Smith:

PricewaterhouseCoopers LLP appreciates the opportunity to respond to the proposed FASB Staff Position (the "Proposed FSP"), *Application of EITF Issue No. 85-24 "Distribution Fees by Distributors of Mutual Funds That Do Not Have a Front-End Sales Charge," When Cash for the Right to Future Distribution Fees for Shares Previously Sold Is Received from Third Parties*. We have the following comments and observations for your consideration.

We agree with the conclusion reached in the Proposed FSP that revenue recognition is appropriate at the time the cash is received from a third party for the Rights (as defined in the FSP) when the distributor does not retain recourse or continuing involvement in the rights. We also agree with the effective date and transition features in the Proposed FSP.

We agree with the staff's interpretation that the condition of no recourse and no continuing involvement is met when neither the distributor nor any member of the consolidated group that includes the distributor (a) retains any disproportionate risk or reward relative to the Rights that are sold; (b) guarantees or assures in any way the purchaser's rate of return on investment relative to the Rights that are sold; or (c) restricts the ability of the consolidated group or the mutual fund independent board to remove, replace, or subcontract any of the entities or individuals providing services to the fund.

We recommend that certain aspects of the FSP and its Basis for Conclusions be clarified in the final FSP, as follows:

- Paragraph 9 states, “no recourse and no continuing involvement is met when neither the distributor nor any member of the consolidated group that includes the distributor...retains any disproportionate risk or reward relative to the rights sold.” The term disproportionate should be clarified to mean, for example, that 100% of the Rights have been sold but 100% of the risks and rewards have not been sold; or less than 100% of the Rights have been sold but the same percentage of risks and rewards have not been sold.
- The last sentence in paragraph 16 states, “Any actual or expected concession by a consolidated group member performing separable services with separate pricing should be presumed to be a service obligation of the distributor.” This statement appears to be at odds with the parallel statement in paragraph 20, “The staff concluded that the services provided by the investment advisor or administrator are separable because the future profit from advisory or administrative services is not affected by the sale of the Rights or retention of the Rights.” We believe the apparent conflict exists because the term “concession” in the sentence in paragraph 16 is unclear. If a service is considered to be a separable service because its profit is unrelated to distribution activities, we believe that service would still be a separable service even though the consolidated group member providing the service has granted (or is expected to grant) a fee concession directly related to that service (thus directly affecting its profitability). We believe that the last sentence in paragraph 16 and its use of the term “concession” was intended to cover situations in which a concession involving the revenues, profits, cash flows, or obligations associated with separable services provided by one or more consolidated group members is directly the result of the transaction between the distributor and the purchaser of the Rights. We suggest that the wording be clarified accordingly. For example, the last sentence of paragraph 16 could read “Any actual or expected concession by a consolidated group member performing a separable service with separate pricing where the concession is directly the result of the transaction between the distributor and the purchaser of the Rights should be presumed to result in the service being a performance or service obligation of the distributor.”
- There are a couple of instances where we believe that terminology relating to risks and rewards vs. continuing involvement should be clarified. Paragraph 18, states that “Continuing involvement exists if the amount received from the third party by the distributor fluctuates as a result of changes in NAV or shareholder redemptions.” If the amount fluctuates, we believe that this form of participation would bear on the transfer of risks and rewards, but would not be a form of continuing involvement because the fluctuation does not result from a service or activity provided by the distributor. As a practical matter, in practice the amounts received from a third party by the distributor are typically fixed at the time of payment. Thus, the sentence in paragraph 18 is generally not reflective of practice. In addition, paragraph 24 states that “providing recourse to the purchaser constitutes continuing involvement.” Although providing recourse alters the

nature of the risks and rewards associated with the Rights, whether it constitutes continuing involvement should depend on the nature of the distributor's activities, as suggested in the balance of that paragraph.

- Paragraph 21 states that "The FASB staff believes the Rights derive from past services provided by the distributor. A distributor is not required to provide any additional service to receive the Rights. That is, if the distributor is terminated or replaced, the mutual fund is still obligated to pay the distributor the Rights . . . If future services are required either by the distributor or by any member of the consolidated group that includes the distributor, revenue should not be recognized when cash is received from a third party for the Rights." We recommend that the last sentence of this paragraph be revised to refer to "future services in connection with the sale of the Rights" to avoid including other services that may be provided by the distributor or another consolidated group member that involve activities unrelated to the sale of the Rights. For example, we understand that the distributor typically authorizes or transfers cash periodically from the fund to the third party purchaser of the Rights. This seems to constitute servicing as defined in FAS 140, paragraph 61, and FAS 140, paragraph 2 includes servicing as an example of continuing involvement. Additionally, the distributor may be required to maintain its status as a registered distributor (e.g., maintain its license) even though it is no longer distributing shares of the fund. We believe the staff intended that these activities of the distributor not be considered continuing involvement, or continuing involvement of a nature sufficient to affect the accounting, because the activities are *de minimis* and require no judgments to be made - unlike, for example, mortgage servicing which involves decisions about collections on individual loans and foreclosures. Our recommended change will help to clarify this.

We appreciate the opportunity to express our views on the Proposed FSP. If you have any questions regarding our comments, please contact Woody Wallace (646-471-2850) or Donald Doran (646-236-7214).

Sincerely,

PricewaterhouseCoopers LLP