

Cleveland, Ohio 44113-2203 (216) 621-6060 Fax (216) 263-4811 Letter of Comment No: 27 File Reference: 1100-LEU Date Received: /0/06/03

October 6, 2003

Mr. Robert Herz Chairman Financial Accounting Standards Board 401 Merritt 7 P.O. Box 5116 Norwalk, Connecticut 06856-5116

Dear Mr. Herz:

Forest City Enterprises, Inc. is a publicly traded real estate corporation headquartered in Cleveland, Ohio with over \$4.0 billion in total real estate assets. We own, develop, acquire and operate commercial and residential real estate across the United States.

We are submitting this letter as a request for the Financial Accounting Standards Board to reconsider certain aspects of Statement of Financial Accounting Standards No. 150 "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity" ("SFAS No. 150"). Although we understand that the issues we have detailed below impact many industries, we have limited our concerns to those that most directly impact the real estate industry. Further, although we understand that the Board intends to issue a delay in the implementation of FIN 46, which we believe has a direct correlation with SFAS 150, we would like to point out that even with the delay of FIN 46 we are seriously impacted by SFAS 150 due to the structure of our business deals.

We, like many real estate companies, invest in entities owning real properties that are organized in a partnership structure (or "partnership-like" structure such as a limited liability company). By practice, or as required by certain state reporting statutes, these entities often have finite lives, often extending 99 years, and providing for further extension. To the extent that we control these investments (prior to adoption of FIN 46, which is discussed below), the assets and liabilities of such investments are consolidated, with the non-owned investor's portion reflected in the mezzanine section of the balance

sheet as minority interest. Prior to SFAS 150, the balance of our minority interest reflected the *book value* of our outside partners' claim on the net assets of our Company.

We understand that pursuant to the provisions of par. 9 of SFAS 150, effective for our third quarter of 2003, the non-wholly owned consolidated entities described above will meet the definition of a mandatorily redeemable financial instrument, in our consolidated financial statements, as such amounts represent an unconditional obligation redeemable by transferring assets at a specified or determinable date (or dates) or upon an event certain to occur (i.e. upon termination of the finite life entity). Furthermore, the minority interest balance must be reflected at fair value, with offsetting adjustments to earnings.

We would like to highlight to the FASB, for their consideration, scrious concerns that we have surrounding SFAS 150 from both our economic views of the underlying transactions which are creating the issues, as well as accounting considerations.

Concept Statement No. 6 "Elements of Financial Statements a replacement of FASB Concepts Statement No. 3 (incorporating an amendment of FASB Concepts Statement No. 2)" focuses on the "usefulness of financial reporting information in making economic decisions." Upon adoption of SFAS 150, we believe that, as it relates to the presentation and treatment of minority interest as a mandatorily redeemable financial instrument, our financial statements will no longer reflect the actual underlying economics of these transactions. The following summarizes matters that adversely impact the presentation of our financial statements.

- a. Upon adoption of SFAS 150, we will likely record <u>substantial</u> charges, which reflect the impact of the appreciation over the original cost of our real estate assets in these consolidated finite life entities. In certain circumstances, SFAS 150 could virtually erase decades of retained earnings/shareholders equity. We believe that this charge to earnings is inconsistent with our financial performance because such amounts are <u>directly</u> associated with the <u>successful</u> operation of the underlying real estate in these finite life investments. Said another way, the more successful an investment in these finite life entities, the larger the reduction in reported earnings.
- b. It seems inconsistent to us that a liability can be recorded at fair value when the assets that will be used to settle that liability are recorded at cost. Further, that liability will not be settled for its recorded fair value if the fair value of the related assets is not realized.
- c. Although the risk and reward profiles are virtually identical, our Company's financial statements will no longer be comparable to those companies that have either invested in real properties structured in entities with an infinite life (such as a corporation) and/or have joint control with their partners and have reflected such investments on the equity method of accounting pursuant to APB 18. We do not agree that the earnings of a company should be so drastically impacted, in situations in which the risks and rewards of the investments are identical, simply

due to differences in the legal structure of an entity. Further, SFAS No. 94 "Consolidation of Majority-Owned Subsidiaries" (par. 38) states that net earnings in a company's consolidated financial statements should normally be the same regardless of the consolidation method used. We believe that any benefits of SFAS 150, as it applies to reflecting a minority interest liability at fair value (with offsetting adjustments in earnings) in finite life entities, will be severely outweighed by the cost relating to the inability of lenders, investors, and other stakeholders who compare the performance of "like" companies. Furthermore, many of our lending agreements require certain debt/equity and other performance measurements that, as a result of SFAS 150, will result in a covenant violations, which could require additional time, effort and cost to resolve.

- d. In order to move towards a fair value model of valuing assets and liabilities that have historically been reflected at historical cost, we believe further guidance on fair value calculation concepts is warranted to ensure that similar transactions are addressed consistently by companies. For example, the valuation of debt is subject to various different valuation models that could result in drastically different results depending on the methodology used.
- e. In some instances this pronouncement can force the recognition of income where no income or true economics have been realized. For example, assume an entity, ABC Company purchase a \$5,000,000 asset with Debt of \$4,000,000 and equity split equally between two partners, ABC Company who is the controlling partner and a third party at \$500,000 each. Assume this asset was purchased on the last day of ABC Company's third quarter, September 30, 2003. For purposes of valuing the minority interest at September 30, 2003, such amount will be reduced by the partner's "share" of estimated transactions costs, assuming that the finite life entity were liquidated. The reduction of the minority interest, reflected estimated transaction costs, results in an increase to be reported in net income. As we have not created any value simply as a result of entering into this transaction, we ask that the FASB consider this in its review of SFAS 150.

It is our understanding that the Board is moving to a principles rather than rule based accounting pronouncements. However, we have found this pronouncement to be rule-based. We understand the provisions of SFAS 150 are effective for the third quarter end and for most companies, the third quarter is already upon us. We hope the Board will take these points into considerations and provide us with a response as quickly as possible. Further, SFAS 150 has a direct correlation with FIN 46, which we believe most companies will be able to defer for one quarter, as many entities that would not have been consolidated under APB 18 may now be consolidated under FIN 46 and vice versa thus impacting the total amount of the consolidating company's minority interest. While we believe an amendment to the pronouncement excluding the provision to fair value minority interest in finite life entities is the correct approach to take, we realize that the Board must follow due process to properly amend the pronouncement. We, like many other companies with our ownership structure are drastically impacted by SFAS 150,

independent of FIN 46. We ask that in the interest of time, at a minimum, the Board consider a delay to the implementation of SFAS 150 until some of the issues we have noted above can be addressed. Please contact us if you have any questions concerning our comments outlined above.

Sincerely,

Forest City Enterprises, Inc.

Thomas G. Smith Executive Vice President, Chief Financial Officer and Secretary

Linda M. Kane Senior Vice President and Corporate Controller

Janet M. Menko Director of Accounting Standards and SEC Reporting