



CardinalHealth

Cardinal Health
7000 Cardinal Place
Dublin, OH 43017
Main 614.757.5000
Toll 800.234.8701

www.cardinal.com

November 24, 2003

Director, TA&I
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Letter of Comment No: 112
File Reference: 1082-300
Date Received: 11/24/03

**Exposure Draft – Proposed Interpretation Consolidation of Variable Interest Entities,
A modification of FASB Interpretation No. 46**

Cardinal Health, Inc. ("Cardinal Health") respectfully responds to the invitation to comment on the *Exposure Draft- Proposed Interpretation to Modify FASB Interpretation No. 46, Consolidation of variable Interest Entities* ("Document"). Cardinal Health is a leading provider of products and services supporting the health-care industry. Cardinal Health, which is headquartered in Dublin, Ohio, employs more than 50,000 people on five continents and produces annual revenues of more than \$50 billion. We appreciate this opportunity to provide you with our views on the Document.

Overall, Cardinal Health is very supportive of the original goal that the FASB was attempting to achieve in drafting FASB Interpretation No. 46, *Consolidation of Variable Interest Entities* ("FIN 46"). We agree that accounting guidance was necessary to moderate the inconsistencies in practice within the marketplace caused by special purpose entities with little business viability, whose sole intent was to keep financial transactions out of a company's financial statements. However, it is our opinion that FIN 46 has swung the pendulum too far in the other direction. As a result, we are now faced with implementing rules that are extremely confusing and in many instances result in financial statements that do not reflect the economic or legal substance of the underlying transactions and business relationships. We do not believe that the Document addresses the numerous concerns expressed by the public, which was provided to the FASB through the comment process. We therefore respectfully request that the FASB delay the effective date of FIN 46 until sound, logical guidance can be crafted. At a minimum, the effective date should be delayed for any variable interest that does not result from an equity investment in the entity. Paragraph A2 of the Document states that FIN 46 clarifies the application of ARB No. 51, *Consolidated Financial Statements* and paragraph A3 states that the mission of the FASB is to improve standards of financial accounting. We would ask you to look at the comments received, the fact that you have had to issue numerous FASB Staff Positions, the fact that you have delayed the implementation date and now have an exposure draft under consideration; all of this is not indicative of guidance that clarifies and improves accounting rules. It is our strong belief that this guidance does not clarify or improve accounting rules. Again, we believe that rules to stop the past practices are necessary but do not believe that FIN 46 accomplishes that objective. Some examples of specific areas of concern are outlined below.

Non-Equity Variable Interests

Many of our serious concerns are centered around variable interests created as a result of normal business activities that do not involve ownership interests. For example, the potential consolidation from variable interests that derive from franchise agreements, loan arrangements or other typical business contracts are conceptually troubling to Cardinal Health. We believe this is an unintended consequence of

the current standard. In the case of loan arrangements, the maximum loss exposure is confined to the amount of the loan outstanding, regardless of the other party's equity investment, loan interest rate, personal guarantees etc. There is already adequate accounting guidance surrounding the accounting for the loan, establishment of any reserves and related disclosures. Why a company should then possibly have to consolidate the entity is troubling. If consolidation was warranted under FIN 46 would the company be able to reverse any related loan loss reserves into income since the outstanding loan has now been eliminated within the consolidated financial statements? What about the creation of a loan as a result of past due trade receivables? Does this now create a variable interest that should possibly be consolidated? These are standard business practices with unrelated entities over which companies have no control. To require a FIN 46 evaluation of these types of transactions seems illogical and is obviously much more than a clarification of previous guidance.

As to franchise agreements, often times the franchisor provides back office services to the franchisee who may be a small independent business person with limited business infrastructure. The franchisee owns and operates his/her business, with assistance from the franchisor to the extent necessary to protect the franchise, but the franchisor has no right to participate in the residual risks or rewards of the business outside of the franchise fee and any loan principal and interest payments. The potential ramifications of FIN 46 requiring the consolidation of these entities would provide very misleading financial statements, since most financial statement users expect that the financial statements reflect the economic assets, liabilities and results of operations that are legally attributable to the entity. This would not be the case with these entities as the franchisor has no legal rights to the activities of the franchise beyond the normal business transactions that occur between any company and its supplier of goods and services.

Entity

FIN 46 is only applicable to entities and paragraph 3 of FIN 46 defines an entity as any legal structure that conducts activities or holds assets. This causes Cardinal Health conceptual difficulties that can be easily demonstrated with a quick example. If Cardinal Health provides a loan to a thinly capitalized LLC to establish a franchise, Cardinal Health would probably have to consolidate this entity under FIN 46. However, as the rules are written, if we made the loan to the individual we would not have to consolidate such transactions under the rules as drafted because an individual is not a legal structure. We question whether the rules are really effective as drafted when they provide for this type of disparity in accounting treatment due to a legal technicality when the economic substance is the same.

Scope Exception for Certain Enterprises That Are Unable to Obtain Information

We believe that the scope exception provided in the guidance for when an entity is unable to obtain information is inadequate. It is presumptuous for the FASB to assume that the issuance of FIN 46 will drive behavioral changes in the business world. To assume that all new business arrangements subsequent to January 31, 2003 will allow for sharing of information required for compliance with FIN 46 assumes too much, in our opinion. Since many of the variable interests are created as a result of business transactions without ownership rights, we believe that subsequent to January 31, 2003 it will still be difficult to obtain access to required information to make a FIN 46 assessment and consolidate if necessary. We urge the FASB to reconsider their belief that parties to all new business ventures will share information in order to comply with FIN 46. The accounting rules should not drive business decisions or force companies to have to turn down business opportunities. We believe that with this scope exception not being applicable to business arrangements entered into subsequent to January 31, 2003 the rules will simply force companies into a position to not be able to comply.

Paragraph 17 – "Activities Closely Associated with the Entity..."

We would like to see additional guidance to help the reader understand the FASB's intent with regard to identifying the party with activities most closely associated with the entity. It is our opinion that this guidance would direct one to look at the day to day activities of the entity in order to ascertain which

variable interest holder had activities most closely associated with the entity. For example, let us assume that a VIE relationship is derived through a loan (i.e. the equity holder obtained his/her equity interest through a loan from another entity, the lender) but the equity holder operates the business on a day to day basis. Let us also assume that the business of the entity is not the primary business of the lender. Under such circumstances, we would understand this guidance to indicate that the equity holder would be the party with the activities (running the business on a day to day basis) most closely associated with the entity, and thus be the primary beneficiary. However, the guidance does not clearly outline what was intended by the FASB when analyzing the concept of activities most closely associated with the entity. Please provide additional guidance and examples to clear up any confusion.

In conclusion, as stated above, Cardinal Health is very supportive of the original goal that the FASB was attempting to achieve in drafting FIN 46. However, based on issues outlined in our letter, we believe that the FASB should delay the effective date, or at a minimum, delay application for any variable interest that does not result from an equity investment in the entity.

Sincerely,

A handwritten signature in black ink, appearing to read "Richard J. Miller". The signature is fluid and cursive, with a small dot above the 'i' in "Miller".

Richard J. Miller
Executive Vice President, Chief Financial Officer