



FSP FIN 46-e

October 6, 2003

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 Financial Accounting Standards Board
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Re: Possible deferral provision of FIN 46

Thank you for the opportunity to comment on the possible deferral provision regarding the application of FASB Interpretation 46, *Consolidation of Variable Interest Entities* (FIN 46), to the asset managers of Collateralized Debt Obligations (CDOs). To provide a timely response, we have included the original proposal received from the staff and inserted our comments in italics in the body of the letter, as follows:

If all of the following conditions exist, the decision maker would not apply the provisions of paragraph 8(c) of Interpretation 46 to that variable interest entity until the Board has completed its consideration of a modification of Interpretation 46 or other accounting pronouncements that may affect those parties.

1. The decision maker has determined that it is the primary beneficiary of the variable interest entity but without applying paragraph 8(c), it would not have been the primary beneficiary

Our thoughts: Paragraph 8(c) is the operative rule that is creating the status of primary beneficiary for the asset manager, so we agree with the concept presented in the above condition. We would prefer language that more specifically addressed this to asset managers. As per the discussion in our comment letter, we believe there is a question as to whether an asset manager providing services to the investors should be considered a decision maker.

2. The variable interest entity's purpose is to invest in financial assets that would be measured in the decision maker's consolidated financial statements at fair value or lower of cost or market or are subject to write-downs for allowances for credit losses, and it has significant liabilities to investors that are reported at the amount of the proceeds ("historical cost") or amortized historical cost.

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Proposed FSP on Interpretation 46 (FSP FIN 46-e)
 Lincoln Financial Group is the marketing name for Lincoln National Corporation and its affiliates.

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Our thoughts: We have no substantive comments on condition 2. Please refer to our prior comments regarding whether there needs to be further guidance as to the status of the asset manager as a decision maker in each of these conditions. This is a common theme throughout our comments and responses, and we will not continue to repeat it to avoid redundancy.

3. The offering documents or debt agreements of the variable interest entity either (a) explicitly state that the decision maker has no obligation to provide financial support to the entity or its investors or (b) explicitly state an obligation to provide financial support that is significantly less than the expected losses of the entity.

Our thoughts: We are not aware of any offering documents that have historically provided the explicit language referred to above. Rather, the deals we are aware of where Lincoln is the asset manager provide specific language that spells out what the specific requirements and responsibilities of the parties are; by reviewing the totality of the documentation, it is clear what the responsibilities of the parties are. If there is no specific language noting an obligation to provide financial support, then the absence of such language would mean that no such obligation exists. We believe an appropriate standard here would require that the asset manager meet a facts and circumstance requirement that, a) it has not contractually agreed in offering documents, debt agreements, or through any other related agreements, to provide financial support to the variable interest entity or to its investors and, b) any specific support explicitly required in the agreements is significantly less than the expected losses of the entity.

We have provided below the type of language that is used in several of the CDO offerings where Lincoln is the asset manager. Other firms may have some differences in the language that their legal counsel will typically use. We believe that this type of language, in conjunction with a review of all the related agreements, should be the type of supporting documentation that would be relied upon in determining whether this condition as been met:

"The obligations of the Applicable Issuers under the Notes and this Indenture are limited recourse obligations of the Applicable Issuers payable solely from the Assets and following realization of the Assets any claims of the Noteholders against the Co-Issuers for any shortfall shall be extinguished. No recourse shall be had against any Officer, director, employee, shareholder or incorporator of either the Co-Issuers, the Investment Manager or their respective successors or assigns for any amounts payable under the Notes or this Indenture. It is understood that the foregoing provisions of this paragraph (i) shall not (i) prevent recourse to the Assets for the sums due or to become due under any security, instrument or agreement which is part of the Assets or (ii) constitute a waiver, release or discharge of any indebtedness or obligation evidenced by the Notes or

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secured by this Indenture until such Assets have been realized. It is further understood that the foregoing provisions of this paragraph (i) shall not limit the right of any Person to name the Issuer or the Co-Issuer as a party defendant in any Proceeding or in the exercise of any other remedy under the Notes or this Indenture, so long as no judgment in the nature of a deficiency judgment or seeking personal liability shall be asked for or (if obtained) enforced against any such Person or entity."

4. The decision maker has no implicit or informal obligation to provide financial support and has not provided financial support in excess of its explicitly stated obligation in this variable interest entity or any other variable interest entity that meets the conditions in this FSP (or to an entity that no longer exists but would have met the conditions at the time of support was provided).

Our thoughts: We agree with the concept that there should be no implicit or informal obligation or commitments to provide financial support. However, we note that in some instances where the returns on the CDO have been below expectations, the asset manager may decide, of their own accord, to reduce the level of fees charged on the deal as a means to maintain its good reputation and relationships with the investors. The amount of such fees waived is insignificant in comparison to the losses allocable to the investors. The decision to reduce or waive fees under such circumstances, which were made prior to the existence of GAAP guidance could create potential issues under FIN 46, but this situation should not pull these deals outside the scope of the proposed deferral of consolidation.

5. If the decision maker consolidated the variable interest entity, it would report losses of the entity in excess of the sum of the following:
- a. The reported amount of the decision maker's equity investment
 - b. The amount allocable to noncontrolling interests in the variable interest entity
 - c. The decision maker's maximum exposure to loss under any explicit obligation to provide financial support to the variable interest entity or its investors.

As long as the deferral for this second circumstance remains in effect, the decision maker would disclose the amounts of assets and liabilities that would have been consolidated if it had applied paragraph 8(c) and would also disclose the information described in paragraph 24 of Interpretation 46.

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Our thoughts: We are confused by condition 5b, because, ultimately, the sum of the reported losses will be those losses attributable to investments made by the asset manager, if any, and the losses allocable to the investors. We do not understand the concept of a decision maker reporting losses in excess of these combined amounts. When discussing losses, it should be clarified whether other than temporary losses effecting net income, as well as temporary losses reflected in other comprehensive income, should be included.

As our comment letter indicates, we are concerned that the asset manager's financial statement would reflect losses on invested assets that have declined in value and that are ultimately allocable to the investors, until such point in the future that the underlying assets are disposed of, the proceeds are allocated to the investors, and the debt otherwise extinguished.

We are also unclear as to whether this condition would only provide a deferral for CDO's that are in an aggregate loss position. As our comment letter indicated, this should be a two-way street, and the asset manager should not be reporting losses or gains that are the investors' gains or losses. Until guidance with respect to these matters evolves, deferral should be provided for CDO asset managers, regardless of whether the deal is a gain or a loss.

While we do not understand condition number 5, we do agree with the need for ongoing disclosure during the deferral period.

In addition to the above comments, we have provided the following response to the following questions that we have excerpted from a second email we received from Ann McIntosh:

This is a message I sent to Casey Trumble yesterday. We would like to know your thoughts on this before our October 8 Board meeting. In addition, I wonder if you could provide some additional information on one of the comments in your September 29, 2003 letter to us. At the bottom of page 6, you discuss the inability of a CDO asset manager to obtain GAAP based financial information on CDOs managed. Could you elaborate on the type of information that is not available to the CDO manager? What efforts have been made to obtain that information? Do the CDOs currently have no obligation to report on a GAAP basis?

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Our reply: Could you elaborate on the type of information that is not available to the CDO manager?

** The CDO asset manager manages the asset portfolio, and has information concerning those assets. However, the books and records are maintained by the administrator. The asset manager may not have access or rights to any detailed financial information outside the assets in the portfolios managed. For instance, the asset manager may not have access to the notes or information as to who owns them, cash reconciliations, receivables/payables, or other non-invested asset balances. The investment manager may not have access to detailed tax records, or income statement accounts. The Trustee has access to information related to the noteholders.*

What efforts have been made to obtain that information?

** Lincoln has been in contact with the administrators to obtain the information. In general, we find that many are not set-up to provide financial information quarterly, or annually, on a GAAP basis. Most have indicated they do not intend to be in the business to provide such services due to a lack of scale. We have also generally found that Trustees do not have the information to provide the service of preparing the GAAP financial statements.*

Do the CDOs currently have no obligation to report on a GAAP basis?

** In general, we find that CDOs have no obligation to report on a GAAP basis, as these are typically non-registered privately held investment structures. Records are typically maintained on a cash basis. Of the CDOs where Lincoln serves as asset manager, two require annual GAAP financial statements; however these are not required to be provided on a timely basis, and have not been historically provided on a timely basis, or on a timetable that would coincide with the accelerated GAAP consolidated reporting timeframe that Lincoln is required to meet. To date, we have not received the 2002 annual GAAP financial statements. The lack of GAAP basis reporting will also impose significant impediments to Lincoln's independent audit processes, as the information needed to provide consolidation information on a GAAP basis may not be in an auditable form or on a timely basis.*

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We appreciate this opportunity to provide comments and clarify the points raised in our previous letters. We would welcome the opportunity to either meet or discuss any questions you might have on the above. As I will be traveling through the 8th, please work with Bob Moose at 215.448.1461 to coordinate any necessary follow-up.

Sincerely,

Handwritten signature of Casey J. Trumble in black ink, followed by a forward slash and the letters 'BT'.

Casey J. Trumble
Senior Vice President Tax & Reporting
Lincoln National Corporation