

NYNEX Corporation  
1113 Westchester Avenue, White Plains, NY 10604-3510  
Tel 914 644 6408  
Fax 914 644 6448

Alan Z. Senter  
Executive Vice President and Chief Financial Officer

Letter of Comment No: 89

File Reference: 1082-154

Date Received: 1/17/96

**NYNEX**

January 15, 1996

Mr. Timothy Lucas  
Director of Research and Technical Activities  
Financial Accounting Standards Board  
File Reference 154-D  
401 Merritt 7  
P.O. Box 5116  
Norwalk, CT 06856-5116

NYNEX appreciates the opportunity to respond to your request for input on the issues identified in the Exposure Draft for the Proposed Statement of Financial Accounting Standards entitled *Consolidated Financial Statements: Policy and Procedures* (the "ED") and we are committed to providing the Board with comments and welcome the opportunity to participate in this process.

In general, NYNEX supports the Board's intent to resolve inconsistencies in industry practice and move toward greater comparability. However, there are areas proposed in this document that NYNEX specifically wishes to address, which are discussed below:

#### **Revised Definition of Control**

NYNEX agrees that the element of control should determine whether an affiliate should or should not be consolidated i.e., if an entity has the ability to use or direct the use of the assets of another entity in the same manner it can use its own, that entity should be consolidated. NYNEX also agrees that in order for an entity to properly present its financial statements the parent company must look beyond the voting interest held in an affiliate in order to determine whether they have control over an affiliate. In fact, NYNEX has been determining its accounting for equity investments based on facts, other than voting interest, that indicate that control over the subsidiary's assets may exist.

#### **Changes in a Parent's Ownership Interest in a Subsidiary**

The Board has determined that the nature of a noncontrolling interest in a subsidiary is part of the ownership equity of a reporting entity, therefore any transactions involving the stock of any subsidiary by any affiliate that does not result in a loss of control is a transaction in the

equity of a reporting entity. As a result, any gain or loss due to the change in a parent's proportionate ownership interest in a subsidiary due to the subsequent purchases or sales of stock by a subsidiary to outside investors through an initial public offering should be an adjustment to equity rather than recognized in the income statement.

Under this method, in the event an entity loses control upon the sale of stock, an entity would only be able to realize a gain or loss in the income statement up to the amount of any additional appreciation or depreciation in the fair market value of the stock subsequent to the initial public offering.

NYNEX feels this topic is not a consolidation issue but rather a *capital stock transaction* and therefore the element of control should not dictate the recognition of a gain or loss, since the basis of this capital stock transaction is the same regardless of the degree of control over an affiliate. NYNEX believes that any gains or losses on this type of transaction, that result in the revaluation of the investment in the subsidiary, should initially be recorded in the equity of the reporting entity as an unrealized gain or loss. In the event there is a loss of control from the sale of a portion of a subsidiary, the true economic gain or loss should be recognized in the income statement since the unrealized gain or loss carried in stockholder's equity will allow the entity to record the gain or loss as a measure of its original carrying value. Although these types of transactions are not within the scope of Statement of Financial Accounting Standards No. 115, "Accounting for Certain Investments in Debt and Equity Securities" (SFAS No. 115) and Statement of Financial Accounting Standards No. 52, "Foreign Currency Translation" (SFAS No. 52), we believe the logic contained in these statements is applicable. In addition, recent information on the Board's project to develop new guidance on the accounting for derivatives has also discussed the recognition of unrealized gains or losses related to the fair value of derivative instruments as a component of stockholder's equity until recognition in the income statement when realized.

Under SFAS No. 115, any unrealized holding gains or losses on securities which are classified as available-for-sale are excluded from earnings and reported as a separate component of shareholder's equity until realized. These gains or losses result from differences between the carrying value and fair value of the debt or equity investment at the reporting date. SFAS No. 115 gains or losses parallel gains or losses that arise from the appreciation/depreciation of a capital investment resulting from the initial sale of stock by a subsidiary to outside investors. In addition, SFAS No. 52 requires that currency translation adjustments resulting from the translation of financial statements in a foreign currency to a functional currency not be included in the determination of net income but be reported as a separate component of equity. Upon the sale of an investment in a foreign entity, the amount attributable to that entity and accumulated as currency translation adjustments as a component of stockholder's equity is required to be reversed and reported as part of the gain or loss on the sale in the period in which the sale occurs.

Statement of Concepts No. 5, "Recognition and Measurement in Financial Statements of Business Enterprises", states that statements of earnings and income should reflect the extent to which and the ways in which the equity of an entity increased or decreased from all sources other than transactions with owners. This is further evidence that gains and losses resulting from a decrease in a parent's ownership caused by the issuance of shares by its subsidiary to outside investors should ultimately be realized in the income statement, since this is not a transaction with owners.

The recognition of a gain or loss in the income statement, currently permitted by the Securities and Exchange Commission under Staff Accounting Bulletin No. 84, is in accordance with the Advisory conclusions in paragraph 30 of the June 3, 1980 Issues Paper, "Accounting in Consolidation for Issuances of a Subsidiary's Stock," prepared by the Accounting Standards Executive Committee (AcSEC) of the AICPA. The staff believes that gain recognition is appropriate where subsequent capital transactions are not contemplated that would lead to concerns about the likelihood of the entity realizing that gain, such as where an entity intends to spin-off a subsidiary. NYNEX believes that gain recognition should continue to be permitted based on this premise, since the change in a parent's proportionate ownership interest resulting from the sale of stock by that subsidiary to outside investors does not parallel a spin-off which is defined as the unilateral transfer of a parent's ownership interest to owners of the subsidiary.

### **Transition**

The Board has determined that retroactive application of the provisions of this statement is necessary unless retroactive application of certain of its provisions is not practicable. NYNEX strongly feels that the provisions of this statement should be applied prospectively with a cumulative effect adjustment as prescribed in Accounting Standards Board Opinion No. 20 (APB No. 20). Any concerns about consistency and comparability with prior years in the balance sheet can be mitigated with required proforma disclosures in the footnotes to the financial statements. NYNEX feels that retroactive application of the provisions of this statement will place an unnecessary increased reporting burden on companies such as NYNEX, without adding any discernible value for the users of those statements. The majority of recently issued accounting pronouncements have required implementation through cumulative effect adjustments and/or additional footnote disclosures. This is in line with the goals of most standard setting bodies to reduce the number of complicated financial statement presentations provided by financial statement issuers that are not of value to users (Jenkins Committee Report). Furthermore, NYNEX feels that this type of accounting change is not of the same magnitude of the types of change outlined in APB No. 20 (correction of an error, change in an entity) which require retroactive application, since whether an investee is reported under the equity method or consolidated the effect on the balance sheet and the income statement taken as a whole is the same in most cases.

## **Conclusion**

NYNEX is in agreement with the Board's definition of control and its use as the basis for consolidation. NYNEX feels that this new method will increase the comparability of financial statements between entities which will be of ultimate benefit to financial statement users. However, NYNEX's proposals, as set forth in the preceding discussion, focus on those areas we believe should be modified to enhance the Board's objectives and are summarized as follows:

- Any gain or loss as a result of changes in a parent's ownership interest in a subsidiary where control continues to exist should be reported as an unrealized gain or loss within the stockholder's equity section since this would result in recognition in the income statement of the entire gain/loss upon sale or liquidation.
- The provisions of this statement should be applied prospectively so as not to create an additional burden to preparers of financial statements that do not provide additional value to the financial statement users.

NYNEX thanks the Board for the opportunity to respond to the ED and welcomes questions concerning the preceding comments.

Sincerely,



Alan Z. Senter  
Executive Vice President and Chief Financial Officer