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Director of Research and Technical Activities
File Reference No. 154-D
Financial Accounting Standards Board
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The Committee on Accounting Principles of the Illinois CPA Society ("Committee"), assisted by the Auditing Services Committee and the Nonprofit Organizations Committee, is pleased to have the opportunity to comment on the Proposed Statement of Financial Accounting Standards -- Consolidated Financial Statements: Policy and Procedures ("ED") of the Financial Accounting Standards Board ("FASB"). The organization and operating procedures of the Committee are reflected in the Appendix of this letter. These recommendations and comments represent the position of the Illinois CPA Society rather than any of the members of the Committee and of the organizations with which they are associated.

The Committee supports the FASB in its efforts to provide guidance in the area of consolidation policy which will conform practice and fill gaps in the current literature and agrees with the fundamental concepts of consolidation as expressed in the ED. The Committee's comments are discussed below.

Accounting for non-controlling interests

The Committee believes the recording of 100% of the fair value of the subsidiary's identifiable assets and liabilities when a parent acquires less than a 100% interest is consistent with the basic theory of control outlined in the ED. However, the Committee was troubled by the grossing up of the non-controlling interest in the equity section of the consolidated balance sheet, i.e., where should the credit go? Some members felt that the situation was amplified in situations in which negative goodwill adjustments are made and also in which the non-controlling interest is a significant percentage. The FASB may wish to reconsider whether the non-controlling interest should be reported between liabilities and equity on the balance sheet, rather than in the equity section.

The Committee would also appreciate clarification on whether the amortization or depreciation of any negative goodwill adjustments would be excluded from the calculation of the portion of net income or loss of a subsidiary attributable to the non-controlling interest.

Conformity of fiscal periods

Paragraph 33 requires "the financial information of a subsidiary in consolidated financial statements shall cover the same fiscal period as its parent's information unless conformity is not practicable." Would the necessity to perform two audits of a subsidiary meet the "not practicable" criteria? This would occur where the subsidiary does not change its year end and must also report separately.

In addition, the ED in paragraph 133 indicates you believe that improvements in telecommunications and management information systems and techniques make the current accommodation no longer necessary. For your information, these improvements have probably not been made to such an extent for many less sophisticated businesses. However, we believe the new "not practicable" criteria would cover these situations.

Effective date and transition

Paragraph 37 requires adoption of the ED for fiscal years beginning after December 15, 1996. The Committee believes that an additional year is necessary to gather appropriate information and to possibly renegotiate agreements which may be dependent on the consolidated entity's financial position. The Committee disagrees with the requirement to restate for the acquisition of a subsidiary, even if practicable. As the Committee expects that restatement for the acquisition of a subsidiary may frequently be not practicable, this requirement will lead to diversity in practice and noncomparability of financial information.

Nonprofit issues

The Nonprofit Organizations Committee has found the level of guidance in AICPA Statement of Position 94-3 ("SOP") to be useful. In particular, this committee believes disclosure requirements with respect to related non-consolidated entities should be retained. The Accounting Principles Committee recommends that any final standard consider and incorporate this guidance where it does not conflict with the basic consolidation principles. Further, as regards nonprofit organizations ("NPO"), the Committee questions how to determine the extent of non-controlling interest. For example, a "parent" is entitled to appoint seven of ten board members of another NPO and thus would consolidate the second entity. Would there be a non-controlling interest of 30% in the second entity presented in the consolidated financial statements?

Another situation of concern is where an NPO has a foundation. The foundation has a self-perpetuating board and the assets are controlled by the foundation, but only to generate income for the benefit of the NPO. The foundation board is not controlled by the NPO and assets would not revert to the NPO. Would this foundation be consolidated? Paragraph 158(f) is an indication that consolidation would be required; however, the other indicators would lead to the opposite conclusion.

Equity accounting

The Committee believes that under current GAAP, the result of applying consolidation procedures has the same income statement result as applying equity accounting procedures. However, the application of paragraph 217(d) will cause a different result between the two methods when accounting for intercompany profits. The consolidated entity will generally not

recognize intercompany profit or loss because the transaction can not be presumed to be at "arm's-length"; however, the same transaction with an equity investee may be recognized in the income statement. If this is the result intended by the FASB, then the Committee recommends the result receive more prominent attention in the final statement.

Auditability

The Auditing Services Committee is concerned that the judgment required in applying the concepts of effective control may lead to significant diversity in practice. They are also concerned about the quality of the evidential matter available to support these judgments.

Other

We also recommend that the second sentence in paragraph 201, "The substance, not just the form of the entity, and the respective transactions must be carefully evaluated," be included in the final standard rather than in an Appendix, given its straightforward stating of the basic tenet of the ED.

We would be pleased to discuss our comments and recommendations with members of the FASB or its staff.

Very truly yours,

A handwritten signature in cursive script that reads "Joan E. Waggoner".

Joan E. Waggoner
Chair of Committee on
Accounting Principles

APPENDIX

ILLINOIS CPA SOCIETY ACCOUNTING PRINCIPLES COMMITTEE ORGANIZATION AND OPERATING PROCEDURES

1995-1996

The Accounting Principles Committee of the Illinois CPA Society (the Committee) is composed of 27 technically qualified, experienced members appointed from industry, education and public accounting. These members have Committee service ranging from newly appointed to 15 years. The Committee is a senior technical committee of the Society and has been delegated the authority to issue written positions, representing the Society, on matters regarding the setting of accounting principles.

The Committee usually operates by assigning a subcommittee of its members to study and discuss fully exposure documents proposing additions to or revisions of accounting principles. The subcommittee ordinarily develops a proposed response which is considered, discussed and voted on by the full Committee. Support by the full Committee then results in the issuance of a formal response, which at times, includes a minority viewpoint.