

Letter of Comment No: 158  
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General Motors Corporation

February 21, 1996

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

Re: File Reference No. 154-D

Dear Mr. Lucas:

We appreciate the opportunity to respond to the Exposure Draft (ED), *Consolidated Financial Statements: Policy and Procedures*. Application of the new consolidation policy and procedures provisions in the ED do not provide more meaningful financial results to users of financial information than the current method, which has been accepted in practice. The "parent company" approach to consolidation, which is present practice, is a practical and objective approach. Consolidation policy and procedures based on an "economic entity" view is a subjective evaluation and a radical change from present practice which we believe will not result in more meaningful information to users of financial statements. As such, we feel it is important to develop consolidation policies and procedures which will preserve the uniformity and consistency in consolidated financial statements. We believe that the ED should incorporate the changes proposed below in accomplishing this objective.

**Consolidation Policy**

We are in agreement that an entity should consolidate all affiliates that it controls for the purpose of reporting the financial state of the reporting entity as a whole. However, the level of legal ownership of a subsidiary must be considered as a strong indicator of control. There should be a presumption of control in the case of a majority equity interest. This presumption can be overcome if other indicators prove a lack of control. Legal or voting ownership is the foundation for control in the business environment. Every parent-subsidiary relationship is based on some form of equity interest, which drives the substance of the control between the two parties (especially absent a harmonious relationship).

In our opinion, the proposed indicators of effective control outlined in the ED greatly increase the subjectivity involved in assessing control. For example, to presume control for an entity which has a minority voting interest assumes that it is possible to determine voting preferences of other shareholders. This results in changes in the consolidation status of subsidiaries from third party actions, such as changes in the voting actions of other parties. This example illustrates how the procedures proposed in

the ED would increase variability in the financial statements of a particular entity over time, as well as increase the inconsistency in the financial statements across different entities. The net assets, net income and cash flows of a particular entity would fluctuate from period to period based on changes in effective control. In addition, there would be different interpretations and applications of effective control across different entities due to the subjective nature of the control requirements. Both of these will result in financial information that is less comparable and therefore, less useful. For this reason, the definition of control in the ED will not provide meaningful results. An objective of the consolidation process should be consistency between different periods and different companies. The purpose of consolidating financial information is to report an entity or group of entities to create a more meaningful picture of the entity as a whole. Allowing subjectivity and interpretation into the process by not focusing on voting interests in consolidation defeats this objective.

In addition to the preceding issue, we have the following comments:

- We agree with the proposal of not requiring consolidation when a parent is obligated or has a plan and reasonable expectation to relinquish control of a subsidiary. The one-year temporary control requirement should be expanded to include an exception from consolidation if it is management's intention to dispose of an entity and there is a reasonable plan to do so, even though the disposal may take more than one year. Additionally, we believe that the display provisions of APB Opinion No. 30, which are discussed in Paragraph 92 of Appendix A, be moved such that the discussion is included in the Statement.
- We strongly disagree with the Board's conclusions in Example 5 of Appendix B which would require the consolidation of a Special-Purpose Leasing Entity. It appears the Board is trying to fix a perceived problem with SFAS No. 13, *Accounting for Leases*, by addressing it in the ED. The Board's conclusion will result in Special-Purpose Entities entering into other transactions to avoid consolidation. This could result in the manipulation of consolidated financial information by changing the business transacted by Special-Purpose Entities in order to achieve the current accounting results. If the Board is unhappy with the results of SFAS No. 13, it should address those issues in the context of that Statement.
- Interpretation issues will occur related to the definition of joint ventures and other unconsolidated entities, which are excluded from the scope of the ED in Footnote 8 to Paragraph 65. Clarification should be provided which defines a joint venture (ownership percentage and corporate structure), to eliminate uncertainty.

### **Consolidation Procedures**

We disagree with the following three consolidation procedures:

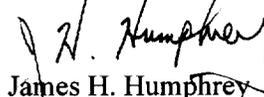
- (1) The allocation of net income between controlling and noncontrolling interests does not improve the value of financial statements to the user. This would not make the statements more useful as shareholders are interested in only that portion of total net income that is available to them. Additionally, we see no compelling reason why the current balance sheet disclosure for minority interest be changed and shown as a separate component of equity.
- (2) We disagree with the proposed accounting for an affiliate that is purchased in a series of separate transactions over time and is subsequently sold. The ED proposes that additional purchases of ownership interest in a subsidiary, which is already considered to be under the control of the parent

(and thus consolidated), be accounted for as treasury stock transactions to the extent the amount paid is in excess of the decrease in the noncontrolling interest. Upon disposition, the result will be a gain or loss different from the real economic gain or loss of the transaction, due to the non-capitalization treatment of fair value over book value on the additional purchases. The substance of the transaction is ignored with the "non-recognition" treatment of such additional purchases. Similarly, decreases in a parent's ownership interest should result in gain or loss recognition, even if it does not result in a loss of control. Recording a gain or loss reflects the true economic substance of the transaction.

- (3) We also disagree with the ED's provision that at the time control is obtained, unrealized holding gains or losses on earlier investments previously carried at fair value and classified as available-for-sale securities be recognized in earnings. The earlier investments are part of the aggregate cost of the acquisition and should be accounted for based on their original costs.

We believe the aforementioned changes to the ED should be made in order to achieve consolidation policy and procedures which are practical to apply and improve the usefulness of financial information. As we feel strongly that legal ownership should be a strong indicator of control, we would be opposed to any policy which would require a company to consolidate debt, for example, which it is not responsible for. If you have any questions or wish to discuss this matter further, please contact me at (313) 556-4167.

Sincerely,



James H. Humphrey  
Chief Accounting Officer