

The Coca-Cola Company

COCA-COLA PLAZA
ATLANTA, GEORGIA

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GARY P. FAYARD
VICE PRESIDENT AND CONTROLLER

January 15, 1996

ADDRESS REPLY TO
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Mr. Timothy S. Lucas
Director of Research and Technical Activities
Financial Accounting Standards Board
File Reference No. 154-D
401 Merritt 7, P.O. Box 5116
Norwalk, CT 06856-5116

Dear Mr. Lucas:

The purpose of this letter is to express the views of The Coca-Cola Company (the Company) concerning the Board's Proposed Statement of Financial Accounting Standard, *Consolidated Financial Statements: Policy and Procedures* (the Exposure Draft).

We have analyzed the proposed accounting included in the Exposure Draft and considered the perceived benefits of reporting additional financial information to our share owners and other users of our financial statements against the cost of compliance. Based on this analysis, we have concluded that the proposed accounting rules, particularly regarding the definition of control, would not enhance the overall usefulness and relevance of our financial statements and, in fact, provide a result that is less meaningful and more costly to implement and maintain than exists under the current rules. Therefore, we strongly oppose the issuance of a new accounting standard that includes the definition of control included in the Exposure Draft.

General Comments

The Board's definition of control as stated in paragraph 10 is as follows:

"Control of an entity is power over its assets - power to use or direct the use of the individual assets of another entity in essentially the same ways as the controlling entity can use its own assets."

We believe that this expanded definition of control is not workable and would replace an objective, verifiable test (more than 50 percent voting interest) with a highly subjective test based on individual facts and circumstances for each potentially controlled entity. In many cases, the subjective decision of whether control exists would be a continuing decision and could result in consolidation decisions that changed from year-to-year based on changes in facts and circumstances without a change in voting interest. This subjective determination of control for less than 50 percent owned entities could result in consolidation of entities over which control does not exist currently or for which control (by definition) may not exist in future periods. Therefore, this could result in misleading consolidated financial statements, create comparability issues within a company's financial statements from year to year and increase diversity in practice.

We believe, as confirmed by our own experience, that we do not have the power to control an entity's assets or direct their use for our own objectives for entities in which we own less than a 50 percent voting interest. The ability to obtain control at some future date due to a unilateral action on our part or by the occurrence of outside events does not mean that we currently have control. The characteristics of control as described in paragraph 10a and 10b (with which we agree) states that control enables a parent to use or direct the use of the assets of a subsidiary by:

- a. Establishing the controlled entity's policies as well as its capital and operating budgets. Capital budgets include, among other things, programs for evaluating and acquiring assets for investment or productive use and for financing those assets through debt, equity or contributions. Operating budgets include acquiring resources other than capital resources and using or allocating all resources.
- b. Selecting, determining the compensation of, and terminating personnel responsible for implementing its policies and decisions.

The ability to control an entity in the future without a majority voting interest, primarily through the active process of nominating and electing a majority of the members of the governing board, does not automatically translate into current control over the entities' operating policies as described above. Therefore, we feel that the Board's linkage of a potential future ability to control an entity with current control as described above is misguided and would lead to inclusion in the financial statements of entities that are not currently subject to the characteristics of control as defined in paragraph 10.

Presumptions of Effective Control

Paragraph 14 addresses the circumstances in which a company may have effective control over an entity in which it owns less than 50 percent of the voting stock. If any one of these conditions exist, effective control would be presumed to exist absent evidence to the contrary. Condition 14a states:

Ownership of a large minority voting interest (approximately 40 percent) and no other party or organized group of parties has a significant interest.

If the Company's investment in an entity met the characteristics of paragraph 14a only, we would have significant influence over the entity and its policies. We understand significant influence to be less directive than the characteristics of control described in paragraph 10 of the Exposure Draft. However, to presume that we would have the characteristics of control over the entity, unless proven otherwise, is a definition of control that is, in our view, an erroneous presumption. Paragraph 157 states:

For example, a presumption of an ability to elect a majority of a corporation's directors with a large minority voting interest may be overcome if the holder's nominees were actually defeated in an election of board members.

Continuing this example, if a company had 4 directors out of 10 on the governing body of a 40 percent owned investee (remaining shares were widely dispersed) they would be presumed to have current control even if there existed no evidence of the characteristics of control (as defined). The proposed rules would have them consolidate the investee since the presumption of control could only be overcome if one of the nominees to the board were defeated in an election. This presumption of control inherently assumes that other share owners that vote with the company or that do not vote must in fact be controlled by the company. We believe this to be a logic error in the Exposure Draft. Once consolidated, this could lead to a hypothetical future situation where the company may attempt to take active, day to day control of the entity by submitting a slate of nominees for election to 6 out of the 10 directors of the governing body. The pursuit of active control could lead the remaining share owners to defeat the nominees and deny the company active control. This confirming evidence of lack of control would occur only after the company had presented the entity as part of its consolidated financial statements.

The consequences of paragraphs 14a and 157 in this example would have required the company to present misleading consolidated financial statements in which they had included the entity (or entities) for the years in which they did not have control. Further, once the confirming evidence of lack of control was received, the deconsolidation of the entity (or entities) would lessen the comparability of the financial statements from year to year. Therefore, we do not believe that a presumption of effective control as indicated in paragraph 14a is workable and could very likely require the consolidation of entities over which control does not exist.

Condition 14b states:

An ability demonstrated by a recent election to dominate the process of nominating candidates for another entity's governing board and to cast a majority of the votes cast in an election of board members.

This condition is even less supportable as a presumption of effective control. It is unclear to us how a company's management could determine whether it is "dominating" a nomination process for candidates for another entity's governing board. Is the mere fact that other share owners vote affirmatively for a company's nominees considered evidence of dominating the nominating process? If so, how could management of the potential parent company possibly produce evidence to the contrary? The Exposure Draft adds almost no insight to this concept which further contributes to the very subjective nature of this presumption.

As to the number of votes cast in an election of board members, the presumption of control is clearly dependent on the number of total share owner votes. This condition could presume control if a company owned a 38 percent voting interest in an entity, voted its entire stake, and the total votes in the most recent election were only 75 percent of eligible votes. What contrary evidence could management provide in this situation to indicate that control does not exist even if there was no evidence of the characteristics of control (as defined)? A further concern that is not addressed in the Exposure Draft is the possibility of future changes in the number of voting and non-voting share owners. Continuing the above example, what would be the proper accounting treatment if, in the next election, 77 percent of the eligible voters cast their votes?

This condition is highly subjective and could result in a continual assessment of the proper application of consolidation procedures. Further, it could also result in different consolidation decisions each year depending on circumstances outside the influence of the potential parent company. For example, past voting patterns are not necessarily indicative of future voting patterns due to changing share owner composition and differing proposals submitted for share owner approval. We believe this is an example of confusing the concept of potential ability to control with actual control.

Condition 14c states:

A unilateral ability to obtain a majority voting interest through ownership of securities or other rights that may be converted into a majority voting interest at the option of the holder without assuming risks in excess of the expected benefits from the conversion.

We believe that the holder of a unilateral ability to obtain a majority voting interest is conceptually closer to achieving actual control than the holder of a potential ability to obtain control. The holder of a potential ability to obtain control usually is required to nominate and elect a majority of the members of the governing body which may or may not be successful. The holder of a unilateral ability to obtain a majority voting interest, as in the case of convertible debt securities, can do so at any time. However, the holder of convertible debt securities generally does not have power over the individual assets of the investee or the characteristics of control (as defined). The ability to achieve the characteristics of control is usually achieved by the act of conversion. For example, the holder of debt securities convertible into a majority voting interest would generally not wish to forgo the cash flows of the debt instrument unless actual control of the entity was desired.

Further, under this presumption of control, an entity owning debt securities convertible into a majority voting interest would be required to consolidate an entity, while a company owning substantially all of the voting stock would not consolidate. For these reasons, we do not support condition 14c as a presumption of effective control.

Indicators of Effective Control

Paragraph 158 of the Exposure Draft lists nine indicators of effective control. Consistent with our comments concerning the presumptions of effective control, we believe these indicators to be inappropriate in making consolidation decisions. In particular, indicator 158g states:

Retention of a significant minority voting interest in an entity after previously holding a majority interest.

In general, many companies sell voting shares in a former subsidiary with the understanding that while the company will retain significant influence with the former subsidiary, control (the power to direct the use of its assets) will also be forgone.

Paragraph 159 states that as more of the listed indicators are present for a potential subsidiary, there is an increased likelihood that control exists. We believe that the characteristics of control as defined in paragraph 10 are generally absent without a majority of voting shares regardless of how many indicators of control listed in paragraph 158 are present.

Relevance, Reliability, and Comparability of Information

The Board's stated objective in paragraph 57 of the Exposure Draft is as follows:

Improvements in the relevance, reliability, and comparability of the information provided by consolidated financial statements will improve their usefulness in assessing an entity's performance and making an investment, credit, or similar decision.

The proposed accounting standard may require a company to consolidate certain entities without owning a majority voting interest and allow other entities in which a similar voting interest is held to be accounted for on the equity method. The different accounting methods used would be determined primarily by subjective determinations and the use of management's judgment. We believe the resultant impact on consolidated financial statements would increase diversity in practice and, therefore, lessen, not improve, comparability.

In addition, the use of different consolidation procedures for entities in which similar voting interests were owned could create confusion to investors and creditors. We believe the potential confusion created by the Exposure Draft regarding the comparability of the reported assets, liabilities, cash flows, etc. would have the opposite effect of the Board's objective by reducing the relevance and reliability of reported financial information.

Further, consolidating certain entities without owning a majority voting interest is inconsistent with the Board's preliminary views regarding disaggregated disclosures. The Board's "management approach" for segment reporting is intended to provide users of the financial statements insight into how management views the business based on information provided in a company's internal financial reporting system. Our Company views less than majority-owned entities, which are primarily bottlers of Coca-Cola trademark products, for internal financial reporting purposes as equity investees. We do not prepare "proforma" consolidations of these investments as this information is not useful or meaningful to management. Therefore, consolidation of certain bottlers which do not report to the chief decision maker and are not viewed as consolidated for internal financial reporting purposes is inconsistent with the "management approach" currently being considered by the FASB for segment reporting.

Our Company's management focus is on the core operations of our business; concentrate and syrup sales to our franchise bottlers. Bottling companies require different management expertise and financial characteristics than does the concentrate business. Bottlers tend to be asset intensive and typically have higher debt-to-capital ratios than the concentrate business. Our currently reported financial statements reflect our primary management focus and the resultant financial characteristics and returns to the users of our financial statements. Accounting for our less than majority-owned bottlers as consolidated entities will diminish the financial characteristics of our

concentrate business and could impact our Company's cost of capital. Further, the resultant financial statements will be less relevant and meaningful to our financial statement users.

In addition, our Company currently consolidates certain bottling operations in which we have a majority interest. Although not our primary long-term business strategy, owning a majority interest in these bottlers allows us to compensate for limited local resources and facilitate improvements in customer relationships while building or restructuring the bottling operations. The key point here from our management's perspective is that when a controlling interest is needed or desired, this is achieved through ownership of a majority voting interest. We believe that active control is operationally achieved through ownership of a majority voting interest.

Benefits and Costs

Paragraph 49 of the Exposure Draft states the following:

The Board believes that this Statement fills a significant need by improving the completeness and thus relevance and reliability of information provided by consolidated financial statements of business enterprises...

The Exposure Draft goes on to discuss the expected costs of complying with the proposed standard in paragraph 51; that these costs will be the incremental cost of revising existing reporting systems to comply with the new requirements and that these costs will not be significant.

We believe that the Board has failed to make the case that the concept of effective control included in this Exposure Draft would improve financial reporting. The concept of a majority voting interest being the primary determinant of control and, therefore, consolidation of a subsidiary is easy to understand and implement and has worked well for the overwhelming majority of companies and the users of their financial statements. Further, supplemental disclosures in the footnotes to financial statements provide additional information to users regarding significant equity investees. We disagree with the Board's view that the benefit of this Exposure Draft "fills a significant need."

Regarding the costs of implementation, we believe that these costs have been underestimated by the Board. We agree that certain financial information is typically requested from equity investees for financial reporting purposes. However, this information pales in comparison to the very detailed financial information required for actual monthly, quarterly and annual results, and the annual and three year budget information that our Company collects. The cost of revising reporting systems would be borne disproportionately by the potential subsidiary. For these reasons, we do not believe the perceived benefits of the proposed accounting standard outweigh the increased costs of compliance.

Our Proposal

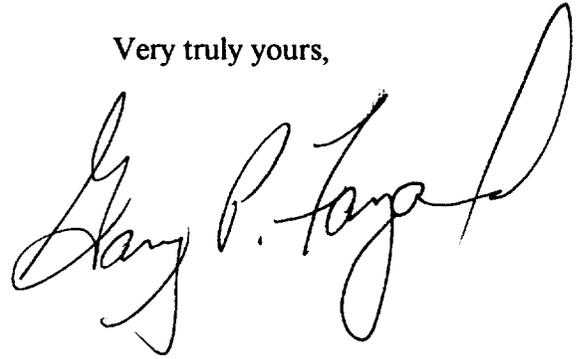
We believe, based on specific facts and circumstances, that control can be achieved with a less than majority voting interest. However, the presumption of control should remain with ownership

of majority voting interest, consistent with the existing guidance under Accounting Research Bulletin No. 51, *Consolidated Financial Statements*. The presumptions of control as listed in paragraph 14 should be considered as “indicators” of control. Control situations should be evaluated in light of the available facts and circumstances and combined with the indicators of control as listed in paragraph 158. The additional guidance would provide management of a potential parent company the ability to determine those situations where control exists with a less than majority ownership.

* * * * *

We would be pleased to discuss any aspects of our views on this project with the FASB or its staff at your convenience.

Very truly yours,

A handwritten signature in black ink, appearing to read "Gary P. Langford". The signature is written in a cursive style with a large, sweeping initial "G" and a long, trailing flourish at the end.