

Letter of Comment No: 97A  
File Reference: 1082-154  
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**NATIONAL ASSOCIATION OF REAL ESTATE COMPANIES**

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Post Office Box 958  
Columbia, Maryland 21044-0958

March 12, 1996

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

**Re: Proposed Statement of Financial Accounting Standards - Consolidated  
Financial Statements: Policy and Procedures**

Dear Sir:

The National Association of Real Estate Companies (the "Association") was pleased to have the opportunity to present to the Board on the Exposure Draft for the Consolidations project "(Exposure Draft)" at the recent public hearing. As a follow-up to that presentation and in response to the Board staff letter of February 28th, the Association would like to offer the following additional observations.

At the public hearing, numerous commentators (including the Association) objected to the Board's conclusion that a controlling entity can use the subsidiary's assets in ways that do not benefit the non-controlling equity interests proportionately. We believe a distinction should be made in the final standard between assets that can be converted unilaterally to the substantial economic benefit of the controlling entity and those whose use is restricted such that they can only be used to indirectly benefit the directing entity in the form of economies of scale or similar efficiencies without the conversion of those assets. In essence, the Association would support the view of one Board member who observed during the hearing that his notion of control assumed that a "substantial" portion of the economic benefits of the subsidiary's assets would flow to the controlling entity. Therefore, the Association would recommend that paragraph 14(f) be removed from the standard and that paragraph 11 be revised to say "a controlling shareholder can unilaterally increase its net cash flows or service potential by initiating actions that result in the use of its subsidiary's individual assets without adversely affecting noncontrolling shareholders' rights to the economic benefits of those assets" (emphasis added). This would yield a facts and circumstances test for consolidation whereby a sole general partner substantively performing as a mutual fund manager would fail.

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This raises the question of how a general partner is similar to a mutual fund manager and what is the nature of the limited partner rights that are usually present in a public syndication that dictate this economic substance. This responds directly to the staff's question regarding shareholder veto rights relative to these types of investor agreements. In most public syndications structured as limited partnerships, the general partner is empowered to manage the affairs of the partnership including initiating transactions to sell or dispose of all or substantially all of the assets of the partnership. The general partner has absolute discretion as to the amount and timing of distributions from the partnership but is required to allocate any such distributions in the proportions specified in the partnership agreement. The limited partners are expressly precluded from participating in the management of the partnership. The limited partners may be given certain rights to veto or approve certain major transactions such as the following: acquisition of significant partnership assets, sale or disposal of significant partnership assets, incurrence of material recourse or non-recourse debt and, material amendment of the partnership agreement. At a minimum, the limited partners are typically able to vote on the removal of the general partner. This vote may require a simple or super-majority and can typically be without cause. This type of removal is comparable to the procedures involved in firing a mutual fund manager. In summary, due to the fiduciary responsibilities and operating parameters under the partnership agreements and partnership law, the sole general partner in a public syndication is similarly restricted in its ability to use the assets of the limited partnership for its own benefit as the mutual fund manager as discussed in paragraph 162 of the Exposure Draft. The key right of the limited partners is the right to remove the general partners without cause. With this right, the general partners operate the assets of the limited partnership solely at the discretion of the limited partnership group. If the limited partners have additional veto or approval powers, this only strengthens the conclusion that the general partner does not have unilateral control of the assets of the syndicated limited partnership.

The Association would agree that there are certain instances where it is appropriate for the sole general partner of a limited partnership to present in its consolidated financial statements the operations of that limited partnership even if the general partner's share of the residual interests is less than 50%. As we indicated in our presentation, these generally are where the structure of the partnership is marginally less than 50% for tax or securities law reasons but the substance of the arrangement is that the general partner has the unilateral ability to dictate the economic destiny of the venture. This type of arrangement is typically the result of a joint venture of a small number of participants and the non-controlling group has delegated to the controlling entity all management responsibility and has intentionally taken a passive role. As long as the non-controlling group is not defrauded, they are willing to allow the controlling entity to make all relevant decisions. Clearly, although an infinite range of economic interests for the general partner between .01% and 49.99% is possible, the reality is that the vast majority of deals fall either very close to 49% or somewhere below 15%. Given this reality and the threshold of APB-18 for the cost method, the Association believes it would be appropriate that the lower limit on economic participation to preclude consolidation could be as low as 20%.

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The Association welcomes this opportunity to further comment on the Exposure Draft. We hope that this additional information will be useful in the Board's further deliberations. As always, we would be happy to discuss any or all of our opinions further with the Board either by conference call or at whatever other mutually convenient opportunity.

Sincerely,

Handwritten signature of Robert A. Wilkins in cursive script, with a small 'SN' or similar mark at the end.

Robert A. Wilkins  
Chairman, Financial Accounting Standards Committee-National Association of Real Estate Companies