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Herbert V. Ryan
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Mr. Timothy Lucas
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Letter of Comment No: 79
File Reference: 1082-194R
Date Received: 5/28/99

Subject: Exposure Draft – Consolidated Financial Statements: Purpose and Policy (File Reference No. 194-B)

Dear Mr. Lucas:

Pfizer Inc appreciates the opportunity to express its views on the FASB Exposure Draft, "Consolidated Financial Statements: Purpose and Policy" (ED), dated February 23, 1999.

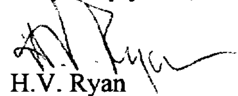
Pfizer is a research-based health care company with global operations in over 140 countries. The Company's 1998 revenues were approximately $13 billion and its assets are approximately $ 18 billion.

We do not support the issuance of the ED as a final Statement of Financial Accounting Standards because we believe the approach in the ED will introduce a high degree of subjectivity into the consolidation decision that could reduce consistency in application and comparability of financial statements among different entities. Moreover, we do not view the Board's proposal as a substantial and necessary improvement over the consolidation policy requirements in ARB No. 51 and FASB Statement No.94, *Consolidation of all Majority-Owned Subsidiaries* (SFAS No. 94). SFAS No. 94 requires that the usual condition for a controlling financial interest is ownership of a majority voting interest, an objective measure, and all majority-owned subsidiaries must be consolidated.

In our view, existing accounting standards, supplemented by disclosures required of SEC registrants with large investees, in most cases, will provide adequate information for users of financial statements.
Under current accounting rules, entities that fall below 50 percent ownership are not consolidated. However, the application of the equity method under APB Opinion No.18, *The Equity Method of Accounting for Investments in Common Stock* (APB No.18), results in the same net income and same net assets as if the 20 – 50 percent owned investee were consolidated. A principle criticism by financial statement users is that, for entities below 50 percent ownership, the investor can omit from consolidation the liabilities of related companies that could materially impact consolidated debt to equity ratios. Under current SEC regulations, separate financial statements must be filed for material investees that are 50 or less owned and accounted for by the equity method. Therefore, users of financial statements have information about the liabilities of related but unconsolidated companies.

Attached are our comments regarding the issues 1 and 2 included in the "Notice to Recipients of This Exposure Draft."

Very truly yours,



H.V. Ryan

Attachment

cc: Mr. D. L. Shedlarz, Senior Vice President - Chief Financial Officer, Pfizer Inc

Attachment
Exposure Draft-Consolidated Financial Statements: Purpose and Policy (File Reference No. 194-B)

Issue 1:

The revised definition and descriptive guidance in the ED is somewhat of an improvement over the definition of control in the October 1995 ED and may be helpful in clarifying when one entity controls another. By broadening the focus in the definition of control from "individual assets" to policies and management, confusion could be minimized in some situations where restrictions may exist on a particular group of assets without depriving the parent's overall ability to direct the subsidiary's assets and ongoing activities.

We note that the October 1995 ED (paragraph 10) states that control enables a parent to use or direct the use of the assets of a subsidiary by (a) establishing its policies, including its capital and operating budgets, and (b) selecting, determining the compensation of and terminating personnel responsible for implementing its policies and decisions. The Board concluded in that ED (paragraph 76) that "this Statement...affirms that being able to direct the management and operating and financing policies of another entity is an essential characteristic of control..." Thus, in our opinion, application of the revised definition of control, together with the descriptive guidance, to a set of facts and circumstances would, in most cases, not result in conclusions different than if the definition (and descriptive guidance) in the October 1995 ED were applied to the same set of facts and circumstances.

We believe that the revised definition of control and descriptive guidance is sufficiently clear and operational. However, we continue to take the position, as stated in Pfizer's response to the Board's Exposure Draft – *Consolidated Financial Statements: Policy and Procedures*, dated October 16, 1995, that control and ownership are two separate and necessary conditions for consolidating a subsidiary with its parent. SFAS No. 94 sets forth a majority ownership threshold, which we believe is appropriate and has worked well in practice.

Issue 2:

The following comments reflect our general agreement with the alternative view expressed in paragraphs 248 – 256 of the ED.

We believe that control should be presumed when an entity has a majority voting interest in the election of a corporation's governing body or a right to appoint a majority of the members of its governing body. This presumption should be evaluated and rejected if there are conditions that would prohibit the majority shareholder from exercising control over an entity. We do not agree that the facts or circumstances described in situations (b), (c) and (d) provide a reasonable basis for presuming that one entity controls another in the absence of evidence that demonstrates or proves otherwise.

We do not believe it is appropriate to presume that there is a control relationship if an entity has a large minority voting interest in the election of a corporation's governing body and no other party or organized group of parties has a significant voting interest. Paragraph 18 of the ED indicates that a minority interest is deemed to be large when it exceeds 50 percent of votes typically cast in election of corporation's directors. As a result of shifting voting patterns of other shareholders, an investor's minority interest may constitute a "large" minority interest in one year (and be consolidated) and not meet that threshold the next year (and be deconsolidated). Past voting patterns may not necessarily be indicative of future voting patterns by shareholders. Accordingly, the application of the presumption of control of situation (b) in paragraph 18 may diminish consistency in the reporting of consolidated financial statements. Additionally, an investor with a large minority interest may not always be aware of actions taken by groups of other shareholders in that investee company to organize and constitute a "significant" voting interest. The fact that a group of shareholders organizes to constitute a significant voting interest might not be revealed to the investor with the large minority interest until the annual meeting of shareholders. If the investor possessed the knowledge of the organized group of investors with a significant voting interest at the year-end preparation of the consolidated financial statements, than the presumption of control would not have been met and the large minority interest would not have been consolidated.

We reject the presumption of control for situation (c) in paragraph 18 of the ED. Absent actions on the part of the holder of the convertible securities or other rights, there often will not be sufficient evidence to demonstrate whether control exists. It is our view that, in many situations, practical difficulties may arise in determining whether the expected benefit

from converting those securities or exercising those rights to obtain a majority voting interest will exceed its expected cost. The cost to exercise a right or option to acquire voting shares of an entity is measured by the cash outlay. But what is the expected cost of loss of
the security of a creditor position (and entitlement to interest payments) which results from the conversion of debt into voting common stock of an investee company? In addition, certain expected benefits such as synergies to be realized between the parent and subsidiary, may not be easily measured. Thus, it may not always be readily determinable whether the unilateral ability to obtain a majority voting interest is sufficiently economic to make its occurrence probable. Moreover, if in one year an entity meets the presumptions in situation (c) and the "parent" consolidates the subsidiary, but in the next year the expected costs from converting those securities exceed the expected benefits, should the subsidiary be deconsolidated? We question the operationality of this presumption of control and believe that its application could result in year-to-year changes in the companies that constitute the consolidated entity.

We note that under APB No. 18, the determination of whether an investor should be presumed to have the ability to exercise significant influence over an investee is based on an investor's currently outstanding voting stock interest. Potential voting privileges that may become available to holders of securities of an investee should be disregarded (paragraph 18). For example, where an investor holds 10 percent of the voting stock of an investee and also holds convertible preferred stock that could be converted into an additional 15 percent voting stock interest, the investor would not be presumed to have the ability to exercise significant influence over the investee. APB No. 18 did not recognize the existence of "latent" ability to exercise significant influence through exercise of convertible securities. By extension, we believe it is inappropriate to recognize the existence of "latent" control through convertible securities before the ability has been demonstrated.

We do not agree with the presumption of control for situation (d) in paragraph 21. That is, in the absence of evidence that demonstrates otherwise, the existence of control of a limited partnership shall be presumed if an entity is the only general partner in a limited partnership and no other partner or organized group of partners has the current ability to dissolve the limited partnership or otherwise remove the general partner. In many cases, it may not be possible to clearly determine whether the limited partners have the current ability to dissolve the limited partnership or otherwise remove the general partner. Absent actions on the part of the limited partners, the current ability to remove the general partner remains uncertain. The determination of whether a general partner has control over a limited partnership should be based on all the relevant facts and circumstances (e.g., terms of partnership agreement, the number of and dispersion of limited partners, etc.), rather than on a presumption and expectation about untested future events.