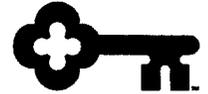


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May 24, 1999

Mr. Timothy S. Lucas
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Letter of Comment No: 30
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File Reference 194-B
Comment on Exposure Draft of Consolidated Financial Statements

Dear Mr. Lucas:

Key Global Finance ("KGF"), an affiliate of KeyCorp, appreciates the opportunity to review and comment on the Exposure Draft of the proposed Consolidated Financial Statements: Purpose and Policy published on February 23, 1999. The proposed statement will have significant implications for the leasing industry. The concern of KGF is that the proposal may not necessarily achieve the desired results of the Board for greater consistency in financial reporting. Furthermore, we believe that current rules provide clear and adequate guidance on the consolidation of entities and that it is not necessary to modify the practice as it exists today.

Key Global Finance and its affiliate, KeyCorp Leasing, are engaged in structuring, arranging and investing in structured asset financing, including leasing. The combined organizations originate approximately \$5 billion in new financing each year. Our activities include a wide variety of structures including single investor and leveraged leases, true leases and finance leases, securitization and project finance. Many of these transactions involve the use of SPEs, each of which would need to be re-examined in light of the new proposal on consolidation if the standard is applied retroactively.

This letter contains our comments on the Exposure Draft as it specifically relates to leasing activities. We believe that the proposed statement would have the following effects for lessees and lessors:

- Inconsistency in treatment of leases with identical characteristics due to the use of a special purpose entity (SPE);
- Inconsistency in practice due to the high degree of judgment required to ascertain control of an entity;
- Conflict with existing accounting standards that provide clear and objective direction.

As a result of these issues, the proposed statement would not lead to significantly more informative or consistent financial statements than under current accounting practice.

Reasons for the Use of Special Purpose Entities

SPEs are commonly used by KGF in structured transactions to achieve a variety of purposes, the thrust of which is to create a broader universe of investors, thereby creating a more competitive financial environment. For example, many forms of securities require the use of bankruptcy-remote vehicles for investment. In leveraged leases, lenders frequently demand that the owners of equipment use an SPE to insulate themselves from the bankruptcy of the lessor. Often, certain institutions such as insurance companies are prohibited from investing directly into the ownership of an asset, or may be subject to higher regulatory capital or taxation as a result, which would not otherwise be applicable if the investment is made indirectly. Frequently, investors in the ownership of assets like to insulate themselves from direct liability from environmental or casualty events; in those cases, the investors are afforded better legal protection through an indirect investment. Also, foreign ownership of aircraft and vessels can be achieved exclusively through an indirect vehicle.

For all of the above reasons, the use of SPEs has become increasingly common as the flow of capital has increased across international boundaries and into new classes of investment. The existence of SPEs does not necessarily change the nature of the intended investment risk assumed by an institution or investor. However, the consolidation draft may cause two otherwise identical transactions to be accounted for differently simply because of the existence of an SPE. As a result, disparities in accounting may occur.

We also have comments on some of the examples in the Exposure Draft. Example 8 illustrates a case that results in non-consolidation of the SPE by the unrelated investors that share control of ABC Trust while Company LE and the trustee are each deemed not to control the Trust. This example is more representative of practice than Example 7 of the Exposure Draft which is recognized as Example 5 from the original Exposure Draft on Consolidated Financial Statements dated October 16, 1995. While Example 8 comports more closely with existing practice, there are many other constructions of transactions for which this example may not shed adequate light. For example, what if the lease is not leveraged, or only a single investor in the Trust existed? Finally, as has been pointed out earlier, what if in all other respects a transaction identical to Example 7 existed except for the use of a trust? While we recognize that it is not possible for the Board to anticipate every possible structure, it would be helpful to provide additional guidance on commonly conceived transactions rather than relying on judgement.

Need for Subjective Decision-Making with New Standard

The proposed standard on consolidation has attempted to provide a new and clearer definition of control over an entity and has focused on the party that has the exclusive ability to make decisions that increase the benefits and limit the losses of an entity. While the Board's goal of determining who would enjoy the economic risks and benefits is admirable, the decision process involves a tremendous amount of often subtle and subjective determinations. As a result, it is quite possible that different reviewers of identical situations could reasonably draw opposing conclusions. Leasing transactions may be particularly problematic because of the variety of options and decisions provided in these situations. We question whether there will be a need for a myriad of interpretations similar to the pooling-of-interest method of accounting.

Application of and Conflict with Existing Accounting Rules

A vast body of literature has developed over the years affecting leasing beginning with SFAS 13. Over time, this literature has gained greater and greater specificity for application. These rules have arisen because of the demand and need for concrete guidance that is not dependent on the reasonable view of varying practitioners. This literature in its application has provided greater uniformity in financial reporting as a result. Although the proposal's impact on existing standards is documented, we have concerns over the applicability of the various EITF consensuses. If this consolidation draft is adopted, it is unclear how the existing standards would be applied, if at all. For example, EITF 90-15 and subsequent clarifications under EITF 96-21, 97-1 and 97-10 provide a level of detail that surpasses the general provisions of the proposed statement. How would the existing rules be applied in light of the new consolidation statement?

Retroactive Application

Existing leasing transactions using SPEs would need to be carefully re-examined in light of the proposed standard. These transactions were conceived with lessors being deemed the owners of assets and consolidating them on their balance sheets. An owner of an SPE has accomplished this treatment with the use of existing rules that require a substantive equity investment. In order to maintain the originally conceived accounting treatment (most often, operating leases for the lessee), it is possible that considerable effort and expense may be required to seek accounting advice, modify legal documentation, possibly eliminate or amend the organizational papers of existing SPEs, and re-record security interests and mortgages. All of this work is achievable. However, the cost of these modifications could be significant, anywhere from 1 to 5% of the original cost of the asset.

In conclusion, we do not believe that adoption of the new statement on consolidation will necessarily result in more consistent financial reporting of leasing transactions. Furthermore, it may provide barriers to investment that would necessarily result in less competition and higher investment costs.

Sincerely,

Mindy Berman

[submitted electronically – no signature included]