# KAUFMAN <u>△</u> BROAD

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William R. Hollinger Vice President and Controller Kaufman and Broad Home Corporation 10990 Wilshire Boulevard Los Angeles, CA 90024 Letter of Comment No: 2 7
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Director of Research and Technical Activities File Reference No. 194-B Financial Accounting Standards Board 401 Merritt 7 P.O. Box 5116 Norwalk, Connecticut 06856-5116

#### Dear Sirs:

I am writing to offer my comments on the revised Exposure Draft of the proposed Statement of Financial Accounting Standards, Consolidated Financial Statements: Purpose and Policy, issued in February 1999, which would establish standards for when entities should be consolidated. As both a provider and user of financial statements, I am impacted by the accounting rules related to consolidation. I have, therefore, been following the Financial Accounting Standards Board's efforts to develop new guidance in this area and wish to express my views on the current proposed Statement.

I have read the revised Exposure Draft of the proposed Statement of Financial Accounting Standards, Consolidated Financial Statements: Purpose and Policy and am opposed to the proposed Statement. My concerns, which relate to the definition of control and its implementation guidance as well as the transition and implications for interim reporting (Issues 1, 2 and 3 of the Notice for Recipients of This Exposure Draft), are discussed below.

#### **Definition of Control and Its Implementation Guidance**

<u>Issue 1:</u> The proposed statement would define control as "the ability of an entity to direct the policies and management that guide the ongoing activities of another entity so as to increase its benefits and limit its losses from that other entity's activities."

The proposed Statement requires that a controlling entity consolidate all entities that it controls unless control is temporary at the time the entity becomes a subsidiary. Thus, the definition of control, as provided in the proposed Statement, is key in making the determination as to whether or not consolidation is required. In my opinion, the definition of control in the proposed Statement is conceptual in nature and difficult to apply in practice since it does not provide an objective and verifiable test to determine when control exists. While in many cases the absence or presence of control of another entity will be apparent, in other cases, highly subjective

determinations based on characteristics which can change from period to period will be required if the proposed Statement is finalized. In contrast to the proposed Statement, the current guidance applicable to consolidation accounting, Accounting Research Bulletin No. 51, Consolidated Financial Statements (ARB No. 51) provides an objective test to determine when one entity controls another entity for financial reporting purposes.

In my opinion, the subjective judgement required in making the determination as to whether control exists will lead to inconsistent application of the proposed Statement and lack of comparability in financial reporting in practice. In my opinion, the proposed Statement, as drafted, does not improve upon the existing guidance provided by ARB No. 51 or clarify when one entity controls another entity. For all of these reasons, I am opposed to the issuance of the proposed Statement.

### <u>Issue 2</u>: The proposed Statement would provide guidance for applying its definition of control.

The guidance provided in the form of rebuttable presumptions of control in the proposed Statement does not, in my opinion, provide a reasonable basis for presuming that one entity controls another entity. Specifically, the presumption that a 1 percent general partner should consolidate a limited partnership would not, in my opinion, result in more meaningful financial statements. I believe that a substantial financial interest should be required for an entity to be consolidated. In addition, the presumption that control exists just because an entity has ownership of 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 interest would also not improve the quality of financial statements.

## Transition and Implications for Interim Reporting

<u>Issue 3</u>: This proposed Statement would be effective for financial statements for annual periods beginning after December 15, 1999, and all interim periods.

In the event the proposed Statement is issued as currently drafted, I believe that the effective date should be one year later than proposed. The implementation of the proposed Statement would require careful consideration and preparation on the part of companies adopting it, particularly in situations where restatement of financial statements for earlier periods is necessary. The effective date as currently proposed would not provide companies with adequate time to evaluate the implications of the proposed Standard and complete its implementation. Therefore, I encourage the Financial Accounting Standards Board to adjust the effective date.

I appreciate the Financial Accounting Standards Board giving me the opportunity to express my comments on the proposed Statement. I am aware that the views I have offered are shared by many others in the accounting profession and that these same arguments may have been heard by your organization before. Nevertheless, due to the importance of this proposed Statement and its potential impact on providers and users of financial statements, I wanted to personally contact you in order to be counted among the many who oppose the proposed Statement.

Please	consider the	opinions of	expressed	above as	you furthe	r evaluate	the revised	Exposure	Draft.
Thank	you for your	attention	to this ma	tter.				-	

Sincerely,

William R. Hollinger Vice President and Controller