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Re: File Reference No. 2011-220

Dear Ms. Cosper:

Grant Thornton LLP appreciates the opportunity to comment on proposed Accounting Standards Update (ASU), *Consolidation (Topic 810): Principal versus Agent Analysis*. We appreciate and support the Board's efforts to (1) address concerns that investment managers and other similar entities would have been required to consolidate certain funds that they manage, (2) address inconsistencies in evaluating kick-out and participating rights between the variable interest and voting interest consolidation models, and (3) converge the principal/agent guidance with that issued by the International Accounting Standards Board. However, we have significant concerns about the proposed ASU in its current form. In summary, our primary concerns are as follows:

- The proposed guidance lacks a clear principle as to how the three factors that should be considered for determining whether a decision maker is using its decision-making authority in a principal or an agent capacity should be weighted. This guidance has been left to examples that provide guidance primarily on securitizations, structured investment vehicles, and investment companies. Only three of the fifteen examples in ASC 810-10-55 would relate to entities outside of the financial services industry. This approach fails to recognize the broad spectrum of entities to which the variable interest model applies. We believe that the Board should develop a clear principle that serves as a basis for determining whether a decision maker is acting as a principal or agent and how the three factors should be weighted. Without a clear principle as to how the factors should be weighted, we believe there will be inconsistent application of the proposed guidance to situations that do not fit clearly within the examples in ASC 810-10-55.
- In our view, the concerns raised by constituents of investment managers and other similar entities represent a narrow population who believe that consolidation under the variable interest model does not present meaningful financial information for the users of their financial statements. We note that constituents of private companies have long expressed similar views and have asked the FASB to address specific concerns related to whether the variable interest entity (VIE) model presents meaningful financial information. We believe these concerns should be addressed.

- We believe that there are practice issues in the application of Statement 167, *Amendments to FASB Interpretation No. 46(R)*, that warrant the Board's consideration. Addressing these practice issues is imperative for consistent application of the existing and proposed changes to the VIE model, as well as for the changes the Board is making to the voting interest model that incorporate various VIE concepts into the broader consolidation model. In particular, we believe that the following two practice issues are of most significance:
  - Reporting entities continue to struggle with the identification of variable interests, in particular, implicit variable interests. The proper identification of variable interests significantly impacts the application of the entire model. For example, we believe that the proposed guidance is unclear as to when one would consider the decision maker's "implicit responsibility to ensure that the entity operates as designed." This is not considered in the Cases for investment funds in ASC 810-10-55; however, it is considered in other examples, such as Case C (ASC 810-10-55-122) for a structured investment vehicle and Case F (ASC 810-10-55-3AY) for commercial paper conduits. Additionally, it is unclear whether voting interest entities would consider implicit interests in the application of the principal/agent guidance.
  - Reporting entities struggle with the determination of the activities that most significantly impact the entity's economic performance and who has power over such activities. This evaluation impacts whether the VIE scope exception in ASC 810-10-15-17(d)(1) applies, whether the entity is a VIE, and who is the primary beneficiary of a VIE. In particular, reporting entities struggle with this evaluation in operating company scenarios. There is no guidance on determining which activities most significantly impact the entity's economic performance other than examples which focus primarily on securitizations and other structured investment vehicles.
- Certain VIE concepts, such as "variability" and "purpose and design," would, under the proposed ASU, apply to voting interest entities. The guidance in the proposed ASU is unclear as to whether such concepts would apply in the same way as in the VIE model. Further, we note that entities such as not-for-profit organizations, for example, would be required to apply the consolidation of partnerships and similar entities guidance that incorporates various VIE concepts for voting interest entities, even though not-for-profit entities are not within the scope of the VIE literature. Not-for-profit entities and other entities may therefore require additional guidance.
- We are unclear when the proposed guidance on evaluating whether a decision maker is using its power as a principal or agent applies in the VIE model. In particular, it is unclear whether this guidance applies only to decision maker contracts that are variable interests under ASC 810-10-55-37 or whether the principal/agent guidance applies more broadly to any situation in which an entity has power. Based on the examples, it appears that the guidance applies more broadly, but we question whether it is necessary to go through a principal/agent evaluation in all fact patterns. For example, a reporting entity could conclude that it does not have power and that it would therefore not be necessary to evaluate the decision maker. As a result, we believe that the principal/agent guidance could be simplified by also considering the evaluation a non-decision maker would go through in applying the consolidation model.
- It is unclear how the proposed principal/agent guidance applies in related-party scenarios and how the principal/agent guidance interacts with the de facto agent guidance.

- All consolidation evaluations, except those that receive a scope exception in ASC 810-10-15-12 or ASC 810-10-15-17, begin with an assessment under the variable interest model. As a result, most principal/agent evaluations would be made under the VIE version of the principal/agent guidance since such an evaluation would need to be made in the evaluation of ASC 810-10-15-14(b). Under the proposed guidance, it appears that the separate principal/agent guidance in the partnerships and similar entities subsections of ASC 810-10 would also need to be applied whenever an entity is determined not to be a VIE. Differences in the VIE model and the non-VIE model would leave open the potential for differences in concluding whether a party is a principal or agent between the two models (for example, because the VIE subsections would require consideration of implicit interests and the non-VIE subsections do not appear to require consideration of implicit interests). As a result, we recommend that the principal/agent conclusion completed as part of the VIE analysis be used as the basis for the general partner evaluation if the entity is determined not to be a VIE and that a separate principal/agent analysis not be required. Under such approach, we believe that the principal/agent guidance in the subsections on partnerships and similar entities would apply only to entities where a scope exception applies, for example, not-for-profits that are scoped out of the VIE model.

We recognize that some of these concerns go beyond the Board's intentions in issuing the proposed ASU; however, we believe that these issues warrant the Board's attention before proceeding with making "limited" changes to the consolidation model. Each time the model is amended, preparers must, at a minimum, go through the process of updating their documentation for changes in GAAP, even if such changes are not expected to change their conclusions. We are also concerned that preparers might have to once again go through the process of reassessing variable interest entity conclusions in the near future should the Board determine that other amendments are needed as a result of addressing private company concerns and/or other implementation issues related to Statement 167. To address these concerns, we recommend that a post-implementation review of Statement 167 be completed, with the objective of determining whether other changes are needed to improve the variable interest model and understanding constituent concerns that the model does not always result in meaningful conclusions. We would be pleased to discuss our experiences on the application of Statement 167 with the Board and staff.

Responses to the Board's specific questions in the proposed ASU

Question 1: When determining whether a decision maker is a principal or an agent, the proposed amendments require the analysis to consider the decision maker's overall relationship with the entity and the other parties involved with the entity. This analysis would be based on a qualitative assessment. Do you agree with this approach? If not, why?

We agree that the principal/agent analysis should consider the decision maker's overall relationship with the entity and other parties involved with the entity. However, the proposed ASU primarily considers the perspective of a decision maker. In other words, if a non-decision maker concludes that it does not have power, would it need to go through an assessment of

whether the decision maker is the principal? We note that a non-decision maker may not have enough information to make such a determination. We encourage the Board to consider the perspective of an entity that can demonstrate it does not have power and to explore how the guidance may be simplified for such an entity.

We believe the proposed guidance lacks a clear principle as to how the three factors in ASC 810-10-25-39C should be weighted in a qualitative assessment. Without more guidance as to how the factors should be weighted, we believe there will be inconsistent application in situations that do not fit clearly within the examples in ASC 810-10-55. ASC 810-10-25-39L states that a decision maker, when evaluating whether its exposure would indicate that it may be a principal, should consider its magnitude of exposure, variability of exposure, exposure to positive returns versus negative returns, and maximum exposure to potential losses. Without providing a clear principle as to how to evaluate the relative significance of different types of economic exposure, we believe there will be inconsistent application in situations that do not fit clearly within the examples in ASC 810-10-55.

We believe that the analysis of whether a decision maker is a principal or an agent should be primarily based on a qualitative assessment. Of course, some situations will require a quantitative assessment, and certain aspects of the existing VIE model may necessitate a quantitative analysis. However, in reviewing the examples in ASC 810-10-55-3B through 55-3BK, the application of the proposed principal/agent guidance appears to depend heavily on a quantitative analysis, without providing context for weighting the factors and considering the extent of compensation and variability from other interests held by a decision maker.

In addition, the proposed ASU lacks guidance as to how the purpose and design of an entity should be considered in determining whether a decision maker is a principal or agent. While the purpose and design is discussed in the examples, it is unclear how such consideration enters into the thought process of determining whether the decision maker is a principal or agent (the purpose and design is discussed in a separate section of the examples). For example:

- It seems that one would differentiate between a decision maker that is involved in the design of the entity and one that is a hired service provider.
- It is unclear how the evaluation would be impacted by a fund manager that provides seed capital that is only temporarily invested.

The discussion below outlines some of our specific concerns/questions with the examples and application of the guidance in ASC 810-10-25:

- Case A (ASC 810-10-55-3G) appears to conclude that "Because the fund manager's interest is pro rata, it is aligned with that of the third-party investors. Considering the purpose and design of the fund, the magnitude and variability of the fund manager's 1 percent fee and 10 percent equity interest, relative to the fund's anticipated economic performance, are conclusive that the fund manager is not using its decision-making authority in a principal capacity." In this example and considering the guidance in ASC 810-10-25, it is not clear whether a significant pro rata interest would change the principal/agent conclusion. In other

words, is more weight given to the pro rata nature of the fund manager's investment or to the magnitude of the fund manager's investment? Is there a threshold in which the Board believes that a fund manager's pro rata investment would be more indicative of a principal relationship? How would one go about evaluating "magnitude"? What if the fund manager had a 40 percent pro rata interest and 1 percent fee, but a single third-party investor had a 45 percent pro rata interest?

- Case B (ASC 810-10-55-3L) could be read to indicate that a performance-based fee of 20 percent is not significant. This will raise questions as to what threshold would such a conclusion change? For example, we believe that currently practitioners consider a 20 percent performance-based fee to be significant in making an evaluation under ASC 810-10-55-37. Alternatively, should the case be interpreted to conclude that because the decision maker was not exposed to negative variability, greater weight was given to that fact in the analysis?
- Case C (ASC 810-10-55-3U) concludes that the fund manager would be a principal based on a pro rata 20 percent interest and the fee arrangement. The conclusion appears to be based on the magnitude of the manager's exposure to variability. However, it is not clear how a reporting entity should evaluate such magnitude. Would there be a different conclusion if another third-party investor has a significant pro rata interest (for example, if party X also has a 20 percent pro rata interest)? How would one think through the proposed guidance in ASC 810-10-25-39L in evaluating this alternative fact pattern?
- The conclusion in Case D (when compared to case C) appears to rest on the fact that a board of directors has substantive kick-out rights over the decision maker. However, Case D also notes that if the fund manager had a subordinate (versus a pro rata) interest, the principal/agent conclusion would be different. Based on this example, it is unclear how the Board intends for the different factors in ASC 810-10-25-39C to be weighted. In other words, why is more weight given to the subordinate nature in the modified example than the substantive kick-out rights? Based on the reference to a situation in which the decision maker also holds a subordinate interest it appears that only kick-out rights held by a single party would be considered substantive. As such, this should be reflected in the guidance in ASC 810-10-25-39D through 25-39H.
- For the cases in which the limited partners in a partnership do not have kick-out rights, would that be an indicator that the general partner is acting as a principal?

Question 2: The evaluation of a decision maker's capacity would consider the following factors:

a. The rights held by other parties
b. The compensation to which the decision maker is entitled in accordance with its compensation agreement(s)
c. The decision maker's exposure to variability of returns from other interests that it holds in the entity.

Are the proposed factors for assessing whether a decision maker is a principal or an agent appropriate and operational? If not, why? Are there any other factors that the Board should consider including in this analysis?

Scope

We believe that in order to appropriately respond to this question, one must understand the scope of the principal/agent guidance. It is unclear whether the proposed guidance on principal/agent is limited only to decision makers that are identified under ASC 310-10-55-37 or whether it applies in all situations a party is determined to have power. While we believe, based on the examples, that the Board's intention appears to be broad, we note that "power" may not necessarily be thought of as only under a decision maker contract. For example, a party may have power through a supply agreement, a sales agreement, rights as a lessee, or a financing arrangement, which do not appear to fit within the proposed principal/agent guidance. If the guidance applies more broadly, we question whether it is always necessary to evaluate whether the entity with power is a principal or agent.

Proposed factors

We do not believe that the proposed factors are operational as currently drafted. As noted above, we believe that the guidance should be improved to incorporate a clear principle that serves as the basis for determining whether a decision maker is acting as a principal or agent.

Additional examples needed

In lieu of a clear principle, the guidance relies heavily on examples that focus on securitizations, structured investment vehicles, and investment funds. We do not believe that the examples included (for a property lease entity, a collaboration–joint venture arrangement, and a furniture manufacturing entity) would provide adequate implementation guidance for the broad spectrum of entities that are subject to the variable interest entity guidance. Even if the Board improves the proposed principal/agent guidance in ASC 810-10-25, we believe that additional examples are needed for other common scenarios, particularly related-party scenarios and VIEs that are operating entities. Such examples should encompass the entire VIE model since many aspects are intertwined. In particular, we believe the examples should include the following common scenarios:

- An expanded related-party leasing example that begins with paragraph ASC 810-10-55-87 to capture other aspects of the VIE model. The example should specifically address whether the common owner would always be considered a principal or whether the manufacturer would be the principal in its stand-alone financial statements. Additionally, we believe that the example should consider an alternative fact pattern in which the property company does not have debt, but the reporting entity has other (implicit) variable interests.
- Other related-party scenarios that involve a common owner, for example, when a common owner owns a manufacturer and a distributor.
- Other related-party scenarios that do not involve a common owner.
- Joint ventures, particularly those established in foreign jurisdictions that require "local equity ownership," real estate joint ventures, and life science joint ventures.
- Fund of funds structures.

We believe that incorporating additional examples is important because non-financial services companies may find it difficult to analogize to the examples that focus on the financial services

industry. For example, the proposed ASU appears to conclude that incentive fees can be considered commensurate with the services provided in evaluating an investment fund. However, the guidance is unclear whether similar arrangements in other types of entities would be viewed similarly. For example, in the life sciences industry, one party may be entitled to receive royalties related to commercial sales or payments contingent on meeting a milestone. Additionally, a real estate developer may be entitled to fees if it completes a project under budget.

We would be happy to elaborate and provide additional examples to the Board and staff for further consideration.

Other factors

We believe that the Board also should consider how this proposed guidance on principal/agent determinations would interact with other GAAP that addresses principal/agent relationships. The following Codification topics provide examples of guidance on evaluating principal/agent relationships or defining an "agent":

- ASC 470-50, *Debt – Modifications and Extinguishments*
- ASC 605-45, *Revenue Recognition – Principal Agent Considerations*
- ASC 860, *Transfers and Servicing*
- ASC 958-10-20, *Not-for-Profit Entities*

In addition, the related-party tiebreaker in ASC 810-10-25-44 currently requires consideration of whether there is a principal/agent relationship between parties within a related-party group. In making the evaluation, some have applied the de facto agent guidance in ASC 810-10-25-43. We note that the guidance on de facto agents has not been amended by this proposed ASU and therefore request clarification from the Board as to whether that guidance applies when making a principal/agent evaluation. Additionally, when evaluating principal/agent relationships under ASC 810-10-25-44(a), some practitioners currently consider the guidance in ASC 605-45. We urge the Board to clarify whether those analogies would continue to be appropriate or to consider whether that guidance should be incorporated into the ASC 810-10 principal/agent guidance; alternatively, the Board could consider whether it would be more appropriate to address principal/agent determinations holistically given the number of situations where different GAAP requires evaluation of principal/agent relationships.

Question 3: The proposed Update would require judgment in determining how to weigh each factor in the overall principal versus agent analysis. Do you agree that the proposed amendments, including the related implementation guidance and illustrative examples, will result in consistent conclusions? If not, what changes do you recommend?

We do not agree that the guidance would result in consistent conclusions. Please refer to our responses to question 1 and question 2 for details.

Question 4: Should substantive kick-out and participating rights held by multiple unrelated parties be considered when evaluating whether a reporting entity should consolidate another entity? If so, do you agree that when those rights are held by multiple unrelated parties, they should not in and of themselves be determinative? If not, why? Are the guidance and implementation examples illustrating how a reporting entity should consider rights held by multiple unrelated parties in its analysis sufficiently clear and operational?

We agree that kick-out and participating rights held by multiple unrelated parties should be considered when evaluating whether a reporting entity should consolidate another party. We also agree that such rights, when held by multiple unrelated parties, should not automatically be determinative. However, we believe further guidance is needed as to how rights held by multiple unrelated parties should be considered. See, for example, our comments on Case D in our response to question 1.

Additionally, we suggest that the proposed guidance in ASC 810-10-25-39G be expanded to provide examples for entities that are not investment companies. For example, reporting entities may assert power in a joint venture scenario is held by the board of directors.

We believe that the guidance on "rights held by other parties" should be expanded to address other rights that a reporting entity may have, such as those relating to budgeting and setting the business plan. For example, a decision maker often may be operating subject to a budget and/or business plan. Further, the decision maker may have various levels of input into the budget and/or business plan, as well as varying levels of discretion in executing the budget and/or business plan. These considerations come up frequently in the evaluation of entities in the life science and real estate industries.

Question 5: The proposed Update would not include a criterion focusing on the level of seniority of a decision maker's fees when evaluating the decision maker's capacity. Do you agree that the seniority of the fee relative to the entity's other operating liabilities that arise in the normal course of the entity's activities should not be solely determinative of a decision maker's capacity? If not, why?

We agree that the seniority of the fee relative to the entity's other operating liabilities that arise in the normal course of the entity's activities should not be solely determinative of a decision maker's capacity. We believe that such exposure to variability should be considered together with other arrangements that expose an entity to variability. However, we believe that it should continue to be a consideration as to whether a decision maker's contract is a variable interest (ASC 810-10-55-37).

Question 6: The evaluation of a decision maker's capacity places more emphasis on the decision maker's exposure to negative returns (for example, an equity interest or a guarantee) than interests that only expose the decision maker to positive returns. When performing the principal versus agent analysis, should the assessment differentiate between interests that expose a decision maker to negative returns (or both negative

and positive returns) from interests that expose the decision maker only to positive returns? If not, why?

We agree that the assessment should place more emphasis on interests that expose a decision maker to negative returns (or both negative and positive returns) than interests that expose the decision maker only to positive returns. However, we are unclear how this guidance interacts with the requirement to evaluate the decision maker's compensation in ASC 810-10-25-39I through 25-39J. We believe that there may be fact patterns (particularly outside the financial services industry) where the decision maker may forgo compensation in exchange for an upside or may agree to provide future services in exchange for an equity interest in the VIE rather than receiving ongoing fees. In other words, the absence of fees or below-market fees could indicate that the decision maker may be absorbing negative variability. Under the proposed guidance in ASC 810-10-25-39J, this would be a strong indicator that the decision maker is a principal. However, under ASC 810-10-25-39K through 25-39L, below market fees do not appear to be negative variability.

Question 7: A reporting entity would be required to evaluate whether there has been a change in the decision maker's capacity by considering whether there has been a change in the purpose and design of the entity. For example, the purpose and design of the entity may change if the entity issues additional equity investment that is at risk to the decision maker. Do you agree with this proposed requirement? If not, please specify when this relationship should be reassessed and why.

We believe separate guidance is not required as to when the principal/agent determination should be reconsidered. We believe that the guidance in ASC 810-10-35-4 as to when to reconsider whether an entity is a VIE and the requirement to constantly reconsider the primary beneficiary are sufficient. Further, ASC 810-20 currently requires constant reconsideration of consolidation conclusions.

We believe that the proposed guidance to reconsider changes in the decision maker's capacity only when there has been a change in the purpose and design of the entity could potentially change the current primary beneficiary determination. For example, in Case E, there may be situations where the decision maker may change when there are multiple levels of subordination (as in a securitization) and the lower levels of subordination are wiped out. Under the proposed guidance, it is unclear how such changes would be considered if the principal/agent determination is reconsidered only when the purpose and design of the entity change.

Question 8: The Board decided to include the principal versus agent assessment as a separate analysis within the overall consolidation assessment, rather than replacing the current guidance for evaluating whether a decision-making arrangement is a variable interest (and accordingly, a principal) with the revised principal versus agent analysis. The Board believes that if an entity's fee arrangement does not meet the definition of a variable interest (for example, a nominal performance-based fee), the decision maker

should not be required to continue the consolidation assessment. Do you agree? If not, why?

We agree that there should be separate guidance as to when a decision-making arrangement is a variable interest and when a decision maker is acting as a principal or agent. For example, a decision maker's related party may guarantee debt of a VIE and therefore have a variable interest, but because a single variable interest holder has unilateral kick-out rights and an equity interest, the decision maker may not be the principal and may not consolidate the VIE under the proposed ASU. However, the decision maker would be required to provide certain disclosures about the variable interest in the VIE.

Question 9: The Board expects the proposed principal versus agent guidance may affect the consolidation conclusions for entities that are consolidated as a result of the decision maker having a subordinated fee arrangement (for example, collateralized debt obligations). However, the Board does not otherwise expect the proposed amendments to significantly affect the consolidation conclusions for securitization entities, asset-backed financing entities, and entities formerly classified as qualifying special-purpose entities. Do you agree? If not, why?

We believe that the impact of the proposed guidance on securitization entities, asset-backed financing entities, and entities formerly classified as qualifying special-purpose entities would depend on the specific facts and circumstances of each entity. In our view, the Board should consider the effects on both existing structures and proposed structures. In general, we believe that the proposed changes to the consideration of kick-out rights could potentially change consolidation conclusions. As noted in the Basis for Conclusions in Statement 167, the Board was concerned that kick-out rights "typically are not exercised and, thus, should not be considered until exercised unless one party has the unilateral ability to exercise those rights." It does not appear that the proposed guidance would require consideration of the probability that kick-out rights would be exercised.

In addition, we believe that the Board should consider the proposed regulations related to securitization risk retention and consider how such changes will interact with the accounting changes being proposed by the Board.

Question 10: Update 2010-10 was issued to address concerns that some believe that the consolidation requirements resulting from Statement 167 would have required certain funds (for example, money market funds that are required to comply with or operate in accordance with requirements that are similar to those included in Rule 2a-7 of the Investment Company Act of 1940) to be consolidated by their investment managers. The amendments in this proposed Update would rescind the indefinite deferral in Update 2010-10 and would require money market funds to be evaluated for consolidation under the revised guidance. The Board does not intend the application of the proposed Update to result in money market funds being consolidated. Do you agree that the application of the proposed Update will meet this objective? If not, why and what amendments would you recommend to address this issue?

We are unclear as to whether the proposed guidance would meet the Board's intentions because the proposed ASU is silent on this issue. The ASU lacks an example that would illustrate how the Board expects the principal/agent guidance to be applied to a money market fund. If it is the Board's intention that money markets not be consolidated, we would prefer that the proposed ASU provide a scope exception for money market funds. Alternatively, if the Board does not believe that the application of the proposed guidance would result in a money market fund being consolidated by a fund manager, an implementation example should be provided to set forth the basis for that conclusion. Key to this conclusion would be the Board's views on how one would assess one's "implicit responsibility to ensure that the entity operates as designed" in evaluating whether a decision maker is a principal or an agent.

Question 11: For purposes of applying the proposed principal versus agent guidance, the proposed amendments would require a reporting entity to include the decision maker's direct and indirect interests held in an entity through its related parties. Do you agree with the requirement that a decision maker should include its proportionate indirect interest held through its related parties for purposes of applying the principal versus agent analysis? Why or why not?

While we agree that it makes sense for a decision maker to include its indirect interests in such an analysis, the guidance may only be helpful with respect to the example provided. There are many other situations in which indirect interests through related parties need to be considered in determining whether a decision maker is acting as a principal or as an agent. Common situations include those in which a principal shareholder or employee of a decision maker entity or a sister entity holds economic interests that need to be considered.

We believe proportionate interests would be appropriate when analyzing a parent and a subsidiary, but not when analyzing the subsidiaries' stand-alone financial statements. In related-party scenarios, it is possible that only the parent has the power and only the subsidiary has economic interests. While this guidance is appropriate in evaluating a parent that is a decision maker, we question whether such guidance is appropriate when a subsidiary has economic interests, especially in situations where the subsidiary issues stand-alone financial statements. As drafted, this change could potentially result in a parent that has power only to be deemed the primary beneficiary without considering the related-party tiebreaker (in other words, a parent would be deemed to meet both the power criterion as a decision maker and the economic criteria through its indirect interest).

In considering our comments, we recommend that the Board consider the applicability of the December 11, 2006 SEC staff speech by Mark Mahar, Associate SEC Chief Accountant, in analyzing when it is appropriate to combine general partner and limited partnership interests.

We also question whether this proposed change is intended to change the definition of "implicit variable interests" to also encompass indirect variable interests. Further, the proposed guidance refers to "indirect interests," a term that is undefined in the proposed guidance. Specifically, the examples included in ASC 810-10-25-96 relate only to ownership interests.

However, it is not clear whether the Board intends for the consideration of indirect interests to mean only indirect ownership interests or to be understood in the context of variable interests.

Question 12: The amendments in this proposed Update would require a general partner to evaluate its relationship with a limited partnership (or similar entity) by applying the same principal versus agent analysis required for evaluating variable interest entities to determine whether it controls the limited partnership. Do you agree that the evaluation of whether a general partner should consolidate a partnership should be based on whether the general partner is using its decision-making authority as a principal or an agent?

Yes, we agree that the evaluation of whether a general partner should consolidate a partnership should be based on whether the general partner is using its decision-making authority as a principal or an agent. However, as noted earlier, we believe that the principal/agent guidance in the partnerships and similar entities consolidation subsection should only apply to entities that would not apply the VIE model.

We note that the principal/agent analysis for partnerships and similar entities incorporates various VIE concepts, such as considering "purpose and design" and assessing "variability"; however, it does not fully incorporate the relevant VIE guidance in evaluating such concepts. Accordingly, it is unclear if the application of the principal/agent guidance for partnerships and similar entities should apply those concepts based on the VIE literature.

Additionally, the VIE principal/agent assessment would require a consideration of implicit variable interests, while the guidance for partnerships and similar entities does not appear to require consideration of implicit interests. We believe that the Board's basis for conclusions should discuss the potential differences in the assessments for VIEs and non-VIEs and, if necessary, incorporate additional guidance in the standard related to the Board's intention.

Further, we note that not-for-profit entities would be subject to the partnerships and similar entities guidance, but not to the VIE guidance. As a result, additional guidance may be necessary for not-for-profit entities in applying the principal/agent guidance.

Question 13: Do you agree with the proposed transition requirements in paragraph 810-10-65-4? If not, how would you propose to amend those requirements, and why? Please provide an estimate of how long it would reasonably take to implement the proposed requirements.

We generally agree with the proposed transition requirements in ASC 810-10-65-4; however, we believe that the transition guidance should be the same as that in ASU 2009-17. Most significantly, we believe that the unpaid principle balance alternative should be permitted.

We also believe that the transition guidance in ASC 810-10-65-2(aaaa) is unclear and confusing. The transition guidance could be simplified if the final guidance resulting from this exposure draft could either be included in a separate section of the Codification or issued in complete

form as part of a final ASU. We note that constituents find the use of pending content to be complicated and often are confused as to the appropriate guidance to follow. Specifically, we note that entities currently applying the ASU 2010-10 deferral would need to analyze each paragraph of the Codification to complete a puzzle that considers pieces consisting of (1) a paragraph that did not change from Interpretation 46(R), *Consolidation of Variable Interest Entities*, (2) a paragraph that was amended by Statement 167, or (3) a paragraph that was amended by this proposed ASU.

We considered an alternative approach which would limit the scope to those entities that were subject to the indefinite deferral in ASU 2010-10. However, we rejected that approach because there are entities that are similar to those that received the deferral in ASU 2010-10 that were not eligible for the deferral because they did not meet the definition of an "investment company." Further, we note that the proposed principal/agent guidance is relevant to entities not targeted by the proposed ASU and therefore any amendments to the principal/agent guidance must consider all entities.

Question 14: Should early adoption be permitted? If not, why?

We are impartial as to whether early application should be permitted.

Question 15: Should the amendments in this proposed Update be different for nonpublic entities (private companies or not-for-profit organizations)? If the amendments in this proposed Update should be applied differently to nonpublic entities, please provide a rationale for why.

We generally believe that GAAP should be the same for public and nonpublic entities. As it relates to this proposed ASU, we note that a majority of the entities targeted by the proposed ASU are nonpublic entities. However, as noted elsewhere in our comment letter, we believe that there are other issues the Board should consider before issuing a final standard, including issues that are of importance to nonpublic entities not targeted in this proposed ASU. We note that in many nonpublic scenarios, including those the Board has targeted in the proposed ASU, preparers do not believe that consolidation produces meaningful results. We believe that the Board should address the concerns raised by nonpublic entities by conducting a comprehensive review of the existing VIE literature to determine whether the consolidation conclusions reached are consistent with the Board's expectation of how the standard would be applied to a variety of entities.

Other comments

Changes to ASC 810-10-25-38A(b)

The proposed ASU would amend ASC 810-10-25-38A to indicate that a decision maker must assess whether it is using its decision-making authority as a principal or an agent. The existing economic criteria in ASC 810-10-25-38A(b) would be amended from the current consideration of scenarios that "could potentially be significant" to consideration of whether a variable interest holder has "the obligation to absorb losses of the VIE or the right to receive benefits

of the VIE." Should proposed ASC 810-10-25-38A(b) be applied based on a materiality assessment or one that considers all possible scenarios similar to current guidance? Or does the Board believe that a reporting entity that is a principal would always be the primary beneficiary? If it is the latter, we believe that it would need to be clear that the principal must have both power and economics. However, as previously noted, we believe that there are scenarios in which a party with power may not think of itself as a principal (as there may not be an agent).

Amendments to the consideration of noncontrolling rights on consolidation

ASC 810-10-25-2 through 25-14, which covers the effect of noncontrolling rights on consolidation, would be amended to more closely align the consolidation requirements for voting interest entities and VIEs. This section has been amended to bring in the VIE concept of the "activities that most significantly impact the economic performance." While we agree with the Board's goal of more closely aligning the consolidation models for voting interest entities and VIEs, we note that the concept of "activities that most significantly impact the economic performance" continues to be difficult for constituents to apply in practice. In order for the amendments to be operational and to improve the existing VIE guidance, we believe that the Board should provide additional guidance on this concept, including additional examples.

Codification

We believe that the consolidation of partnerships and similar entities guidance should remain in ASC 810-20 and should not be moved to ASC 810-10. We note that a primary reason for including the guidance in the same subtopic would be to reduce duplicate guidance; however, such guidance would be repeated in ASC 810-10 for VIE and partnerships/similar entities.

Further, it has been our experience that constituents have found the use of subsections to be confusing. Prior to these amendments, this concern was mitigated in the consolidation topic of the Codification since some constituents simply continued to use Statement 167. This will no longer be possible once these amendments are finalized. We recommend that the VIE literature comprise its own subtopic under consolidation.

Proposed definition of kick-out rights

The proposed ASU would change the existing VIE definition of kick-out rights to "The ability to remove a decision maker of an entity of its decision-making authority or to dissolve (liquidate) an entity without cause (as distinguished from with cause)." We believe that kick-out rights need be carefully evaluated. While ASC 810-10-15-13A requires entities to consider only substantive terms, transactions, and arrangements, such guidance is only applicable to VIEs. We recommend that the guidance in ASC 810-10-15-13A be applicable to all entities applying the principal/agent guidance, including those entities that previously would have applied ASC 810-20.

Codification VIE disclosures inconsistent with Statement 167

ASC 810-10-50-5A provides disclosures that apply to a reporting entity that is a primary beneficiary of a VIE or a reporting entity that holds a variable interest in a VIE but is not the

entity's primary beneficiary (other variable interest holders). ASC 810-10-50-5B provides the following exception to those disclosure requirements:

> A VIE may issue voting equity interests, and the entity that holds a majority voting interest also may be the primary beneficiary of the VIE. If so, and if the VIE meets the definition of a **business** and the VIE's assets can be used for purposes other than the settlement of the VIE's obligations, the disclosures in the preceding paragraph are not required.

Originally, under Interpretation 46(R) this scope exception only applied to a primary beneficiary. However, since this scope exception also applies to disclosures made by other variable interest holders, some constituents have asserted that this scope exception would also apply to the other variable interest holders when they can conclude that the primary beneficiary meets the scope exception. We request that the Board clarify this scope exception.

Potential drafting issues

ASC 810-10-25-39E states: "When a single party (including its related parties) holds a substantive kick-out right (or other rights that have a similar effect on the decision maker's ability to exercise its power) and can remove the decision maker **without cause**, this, in isolation, is sufficient to conclude that the decision maker is an agent rather than a principal." However, we note that the proposed definition of "kick-out rights" in ASC 810-10-20 already relates to rights that can be exercised **without cause**.

We also believe that the definition of kick-out rights linked to ASC 810-20 should be superseded by this proposed ASU.

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We would be pleased to discuss our comments with you. If you have any questions, please contact Mark K. Scoles, Partner, Accounting Principles Consulting Group (Mark.Scoles@us.gt.com or 312.602.8780) or Jamie Mayer, Managing Director, Accounting Principles Consulting Group (Jamie.Mayer@us.gt.com or 312.602.8766).

Sincerely,

/s/Grant Thornton LLP