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December 1, 2003

Director of Technical Application and Implementation Activities
Financial Accounting Standards Board
401 Merritt 7
Post Office Box 5116
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Letter of Comment No: 74
File Reference: 1082-300
Date Received: 12/01/03

Re: File Reference No. 1082-300

Dear Director:

We are writing in response to your invitation to comment on the Proposed Interpretation, *Consolidation of Variable Interest Entities, a modification of FASB Interpretation No. 46* ("Exposure Draft").

KeyCorp ("Key"), headquartered in Cleveland, Ohio, is a bank-based financial services company that, at September 30, 2003, had assets of approximately $84 billion. Financial institutions like Key have been greatly impacted by the accounting guidance in FASB Interpretation No. 46 ("FIN 46") and have spent a significant amount of time interpreting and applying it to various entities. Although Key adopted FIN 46 effective July 1, 2003, we remain very interested in new interpretations and guidance related to this pronouncement because of the potential impact to existing entities and future structures.

We appreciate the opportunity to comment on the Exposure Draft and support the Board's commitment to provide additional accounting guidance and clarification of some of the critical portions of FIN 46. Key takes pride in providing detailed, timely and comprehensive financial information to the investment community, and supports standards and interpretations that clearly result in accurate and useful information that can improve investor understanding and allow for more informed decisions.

Following are Key's comments regarding two specific aspects of the additional accounting guidance set forth in the Exposure Draft.

Reconsideration Events

In Paragraphs 5 and A25 of the Exposure Draft, the FASB has attempted to provide additional guidance to address when a restructuring of the debt of a financially troubled entity by an existing lender could result in consolidation by that lender.

However, instead of providing this additional guidance, Key would recommend adding a scope exception to FIN 46 for lenders that restructure debt of a troubled entity, as defined under FASB Statement No. 15 and related guidance, and for other loan workout situations. Adequate accounting guidance already exists to address the accounting for these situations. Key does not believe that the intent of FIN 46 was to require financial institutions to consolidate borrowers because of actions taken to recover outstanding loan balances. To be consistent with other scope exceptions that the Board has made, this recommended exception should not be applicable if the troubled debt restructuring or workout situation was orchestrated to circumvent FIN 46.

A second but less preferable alternative would be for the FASB to provide more clarification or specific examples as to what constitutes a reconsideration event in a debt restructuring.

For example, it is not clear how a success fee negotiated by a lender in a debt restructuring would be viewed under the Exposure Draft. A success fee represents an amount payable by a borrower to a lender in addition to principal and interest on restructured debt, and is typically payable upon satisfaction of certain criteria or upon the occurrence of certain events (i.e. the sale of the business or certain assets or the refinancing of the debt with another lender). The fees may be fixed in amount or calculated as a percentage of future cash flows or proceeds. Key views success fees as compensation for concessions granted in a restructuring and for bearing increased risk while working out the loan. While such an arrangement does not provide the lender with additional voting rights, under the Exposure Draft, it could potentially be argued that success fees are equity-like in nature and change the characteristics of the equity investment at risk.

We believe the Board should include more specifics or practical examples as to how a debt restructuring can increase a borrower's expected losses or change the characteristics of the borrower's equity investment at risk. Debt restructurings often result in more changes to a loan agreement than simply extending the maturity date or reducing the outstanding balance.

Related Party Tiebreaker

Because of FIN 46's expanded definition of related parties, companies such as Key have had to rely extensively on the guidance in FIN 46's Paragraph 17 to determine which of the legal entities in a related party group, including de facto agents, should be considered the primary beneficiary.

The Exposure Draft replaces the current language in Paragraph 17 of FIN 46 with the following:

> " If two or more related parties (including the de facto agents described in paragraph 16) hold variable interests in the same variable interest entity, and the aggregate variable

interest held by those parties would, if held by a single party, identify that party as the primary beneficiary, the party with activities that are most closely associated with the entity is the primary beneficiary. If two or more parties with variable interests have an agency (or de facto agency) relationship, the principal (or de facto principal) is presumed to be the primary beneficiary unless another party within the related party group has activities that are more closely associated with the entity."

We agree with the Exposure Draft's position that the primary beneficiary should be the party with activities most closely resembling those of the entity, if such a party can be identified. In practice, however, it can be very difficult to determine which party has activities most closely resembling those of the entity. An example of this is when two investors hold substantially all of the variable interests in an entity and both investors are actively involved in the same industry. If neither of the investors has activities most closely associated with the entity and a de facto agency relationship exists between them, the Exposure Draft would require the de facto principal to consolidate the entity. We take exception to the Exposure Draft's new language because we do not believe a de facto principal should automatically be required to consolidate the entity in such circumstances.

Prior to the issuance of the Exposure Draft, we believed that Paragraph 17 provided for the determination of the primary beneficiary within a related party group in the following sequence and priority:

1) the party with activities most closely associated with those of the entity, if such a party is identified
2) the principal in a legal agency relationship, if such a relationship exists within the related party group
3) the party absorbing the greatest amount of the entity's expected losses and/or residual returns, if no legal agency relationship exists within the related party group

Key believes that a de facto agency relationship should not automatically require the de facto principal to consolidate the entity in situations where no party has been identified as having activities most closely resembling those of the entity. A de facto agency relationship, as defined in FIN 46, is not a true legal agency relationship. As such, the de facto agent does not have legal authority to act for the de facto principal and does not follow the directions of the de facto principal. We agree that the existence of a de facto agency relationship requires careful consideration and assessment under Paragraph 17 of FIN 46 and may result in the de facto principal being determined to be the primary beneficiary. This would happen, for example, when a de facto agency relationship results in the de facto principal having the same degree of control over the de facto agent's actions and decisions as a principal would have in a legal agency relationship. In such a situation, the de facto principal would be construed as having activities that most closely resemble those of the entity, making the de facto principal the primary beneficiary. However, depending on the particular facts and circumstances, it may not be appropriate or reasonable to view the de facto principal as the primary beneficiary. Key believes that a quantitative assessment should be used to determine the primary beneficiary when the de

facto agent is an independent third party, is exposed to considerably more of the entity's expected losses than the de facto principal, and acts on its own behalf.

Therefore, Key would suggest modifying the Exposure Draft to indicate that if no party is identified as having activities most closely associated with the entity, and if no legal agency relationship exists, the primary beneficiary is the party absorbing the greatest amount of the related party group's expected losses and/or expected residual returns.

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Key believes that the changes and enhancements suggested above will improve the accounting guidance set forth in the Exposure Draft and should provide readers with sufficient information for interpreting how the principal concepts should be applied in practice to ensure consistency among financial statement preparers and others involved in this process.

We hope these comments are useful and positively influence the final Interpretation. We welcome the opportunity to discuss these issues in more detail. Please feel free to contact Chuck Maimbourg, Director of Accounting Policy & Research, at 216-689-4082 or me at 216-689-3564.

Sincerely,

Lee G. Irving
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