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NATIONAL

Mr. Timothy S. Lucas

ASSOCIATION

Director of Research and Technical Activities

Financ

Financial Accounting Standards Board

OF

File Reference 194-B

REAL ESTATE

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INVESTMENT

Norwalk, CT 06856-5116

Trusts®

Re: Proposed Statement of Financial Accounting Standards - Consolidated Financial Statements: Purpose and Policy

Dear Mr. Lucas:

The National Association of Real Estate Investment Trusts (NAREIT) is pleased to have the opportunity to respond to the Financial Accounting Standards Board's ("the Board") proposed policy on consolidated financial statements. NAREIT is the national trade association for publicly traded real estate companies. Members include real estate investment trusts (REITs) and other businesses that develop, own, operate, and finance income-producing real estate, as well as those firms and individuals who advise, study, and service these businesses. The business of developing, owning and operating income-producing property often involves multiple business arrangements and unique organizational structures. In this context, the policy governing consolidation is important to producing useful financial reports for publicly traded real estate companies.

NAREIT supports the Board's efforts to enhance the usefulness and relevance of financial reporting. However, NAREIT is opposed to the issuance of the standard on consolidated financial statements as proposed in the current February 23, 1999, Exposure Draft. We opposed the original exposure draft and, as the revision is substantively unchanged, our opposition continues.

Our opposition to the consolidation criteria proposed in the current Exposure Draft stems specifically from the Board's insistence that control or effective control, without regard to the materiality of economic ownership, is sufficient

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criteria for one business enterprise to consolidate another business enterprise. We believe that consolidated financial statements should include only those assets, liabilities, revenues, expenses, and cash flows in which the reporting entity has a material economic interest, as well as control.

The proposed standard on consolidations is based on whether a parent has non-shared control and the ability to increase benefits and limit losses. We believe that the Board's approach to consolidations would be strengthened (i.e., made more uniform, meaningful, and transparent) if it included a quantitative economic threshold. In the case of real estate organizations, the proposed policy will not improve the quality of consolidated financial statements. Where non-shared control exists in the absence of a substantive economic benefit, the consolidation inevitably results in a "grossing up" of the financial statements, making meaningful financial analysis all the more difficult.

The following describes the unique general and limited partnership, as well as joint venture arrangements, typical of publicly traded real estate companies. Consolidation issues under these arrangements suggest the need for a benchmark in addition to non-shared control. NAREIT offers a suggested alternative to the proposed policy that is based on both economic benefit and control.

General Partnership Interests in a Limited Partnership

NAREIT is concerned about the potential for "grossing up" the financial statements of a general partner when its interest represents only a nominal economic benefit.

Under the proposed consolidation standard, publicly traded real estate companies may be required to consolidate numerous, previously syndicated, public and private limited partnerships or other special-purpose entities in which they hold a one (1) percent general partnership interest entitling them to a nominal share of the economics. NAREIT is concerned that consolidation of these syndicated partnerships will lead to financial statements that grossly distort the assets, liabilities, revenues and expenses, and cash flows of the reporting entity. Including the assets, liabilities, operations, and cash flows of the ninety-nine (99) percent interest not owned by the general partner in the reporting entity's consolidated financial statements, would diminish the usefulness of the information presented, as well as most summary indicators (i.e., financial ratios). The parent company's financial statements would be significantly overstated, generating a misleading portrayal of the parent company's assets, liabilities, revenues, expenses, and cash flows. Under this scenario, the financial position, operations, and net cash flows that are relevant to the reporting entity and the entity's stakeholders would be difficult for financial statement users to comprehend.

Joint Venture Partnerships

Many publicly traded real estate companies are also engaged in joint venture partnerships in which they hold less than a majority interest. Based on the proposed consolidation standard, a holder of less than a majority interest may be required to consolidate the partnership in its

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entirety in its financial statements. The impact on the financial statements for a nominal general partnership interest also applies to joint venture partnerships. Including interests that do not generate material economic benefit is misleading to shareholders and creditors of the parent company.

Influence on Corporate Structure

We believe that if adopted as proposed, the consolidation standard will have the unintended effect of changing business practices in order to avoid consolidation. The proposed standard would significantly influence how an entity structures the ownership of its business relationships (i.e., joint venture partnerships) so as to provide just enough rights to the other parties, or some type of control mechanism (e.g., approval of annual business plan), so that the entity would avoid consolidation. To overcome this unintended consequence, as well as address shortcomings to the proposed standard as it relates to the consolidation of entities in which the parent owns a nominal interest, we offer an alternative solution below.

Alternative: Minimum Economic Threshold

NAREIT believes that current standards of consolidation as promulgated by the Board and the American Institute of Certified Public Accountants (AICPA) are unambiguous in their application to most corporate, partnership and special-purpose entity situations. We are not aware of instances where assets, liabilities or operations that are significant to the enterprise are not already disclosed in some fashion under current standards.

The proposed standard would require the consolidation of many entities that are currently accounted for under the equity method. Current practice, as specified by Accounting Principle Board Opinion No. 18 paragraph 20 (d), or its analog in AICPA Statement of Position 78-9, already requires the disclosure of the operations of significant equity investments. If the operations were not disclosed because they are not "significant," why would the consolidation of these operations improve financial reporting? Requiring the consolidation of minority-owned subsidiaries would not benefit the users of financial statements. In fact, as we have previously described, it would hinder an analysis of the reporting entity.

Notwithstanding our interest in seeing the proposal being withdrawn completely, the Board may decide to issue a final standard along the lines of the current proposal. As such, we suggest the inclusion of a twenty (20) percent minimum economic threshold to determine when consolidation is considered. In this scenario, a parent would be required to review whether control exists for consolidation when its economic interest in the subsidiary is greater than or equal to twenty (20) percent. If control exists, consolidation would be required, otherwise the equity method would apply. If the parent has an economic interest less than twenty (20) percent, the accounting method would be based on current literature.

Board Issues - Definition of Control and its Implementation Guidance

Issue 1: Definition of control – We are concerned that the proposed definition of control may result in different accounting treatments for very similar factual economic circumstances, leading to inconsistent application and lack of comparability between companies. Criteria that is vague and includes qualitative assessments on whether control exists, changes what is currently an objective decision rule for consolidation into a subjective process, subject to potential manipulation and inconsistency of reporting between companies.

As an example, assume two joint venture partnerships similarly structured in terms of legal and economic substance, with the sole general partner in each having a thirty (30) percent economic interest. In the first situation, there are only two limited partners, while in the second, there are 1,000 limited partners. As proposed, the standard would require consolidation in the latter scenario, due to the wide dispersion of limited partnership interests, but not in the former. Thus, the proposed consolidation policy would result in divergent outcomes for a sole general partner having equal economic interests in two joint ventures.

Further, in the second scenario with 1,000 limited partners, if a separate party acquired substantially all of the limited partnership interests, the proposed standard would lead to the conclusion that consolidation by the general partner would no longer be required. This would result in an erratic consolidation policy, leading to less useful, consistent, and comparable financial statements.

Issue 2: Rebuttable presumptions of control – Although guidance in the form of rebuttable presumptions of control would be helpful, we do not believe that the rebuttable presumptions of control described in (b), (c), and (d) provide a reasonable basis for presuming that one entity controls another entity. We agree with the Alternative View (contained in paragraphs #248 through #256) that the rebuttable presumptions of control are not operational because they "...assume the existence of control without confirming evidence to support their conclusion."

With regard to presumptions (b) and (c), we agree with the view in paragraph #251 that: "...until such time as [the] minority investor actually attempts to change the composition or policies of the investee's governing board, there is no conclusive evidence available to demonstrate that the existing governing board will adhere to or accept policy directives or managerial changes proposed by the large minority investor."

We also agree with the view articulated in paragraph #255 in relation to a sole general partner in a limited partnership, which states in part: "...situation (d) is overreaching because its presumption of control depends on the assumed inaction of the limited partners in situations in which their "current ability" to remove the general partner is uncertain and untested."

Issue 3: Interim reporting – We believe that comparative financial information is fundamental to effective financial analysis, but consider restatement of prior interim periods in this case to be

extremely burdensome. If the Board adopts the standard to be effective for periods after December 15, 1999, it should be applied only to the full year for the year of adoption. As an alternative, we suggest delaying the effective date for implementation to years beginning after December 15, 2000. Companies could then provide for comparative interim periods during 2000.

Conclusion

We would urge the Board to withdraw this revision to the Exposure Draft completely. There were 162 comment letters submitted to the original Exposure Draft issued in 1995. In addition, during two days of public hearings, twenty-six organizations took the opportunity to make oral presentations to the Board. A substantial majority of these respondents (including all of the then "Big 6" accounting firms, the AICPA and the Financial Executives Institute (FEI)) opposed the issuance of the standard. All of these named respondents argued for some sort of minimum ownership threshold to require consolidation. In paragraph #215, the Board suggests that because these respondents did not propose a common level of benefits and/or a common definition or description of the benefits to be measured, the criteria of a minimal level of economic interest would not be appropriate. We believe that given the opportunity, respondents who argue for a minimum economic interest criterion would be able to agree on the level and description of required benefits (e.g., twenty (20) percent minimum economic threshold). Lastly, we believe that objective criteria are essential for achieving relevant consolidated financial reporting.

Sincerely,

Stephen C. Richter

Treasurer, Weingarten Realty

Co-Chair, NAREIT Accounting Committee

Stephen C. Richter/BMT