

February 13, 2012.

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Via email: director@fasb.org

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Re: Proposed Accounting Standards Update, Financial Services – Investment Companies (Topic 946): Amendments to the Scope, Measurement and Disclosure Requirements

Dear Technical Director:

State Street Corporation ("State Street") appreciates the opportunity to comment on the FASB's Proposed Accounting Standards Update, Financial Services – Investment Companies (Topic 946): Amendments to the Scope, Measurement and Disclosure Requirements (the "Proposed ASU"). With \$21.8 trillion of assets under custody and administration and \$1.9 trillion in assets under management at December 31, 2011, State Street is a leader in providing financial services and products to meet the needs of institutional investors worldwide. This comment letter is written from State Street's perspective as both an asset servicer and manager, and the preparer of its own consolidated financial statements.

We support the Board's efforts to develop consistent criteria for determining whether an entity is an investment company, and to improve comparability between U.S. GAAP and IFRS for entities that qualify as investment companies. However, we do not support the Proposed ASU in its current form, and we offer comments herein that we believe propose actions necessary to achieve the proper balance between improving comparability across entities and giving financial statement users more relevant and reliable information to evaluate an entity's financial performance. We hope that the Board finds our comments helpful as it continues to re-deliberate the proposed guidance.

Executive Summary

Investment company accounting provides important and meaningful information to investors in its current form. Nonetheless, we acknowledge there are exceptions where transparency could be improved. The proposed amendments attempt to improve financial reporting for these exceptions; however, these amendments do not enhance, and in some cases dilute, financial reporting for investment companies as a whole by creating new exceptions.

We believe that the determination of an investment company should be a multi-factor, principles-based, qualitative consideration (based on its nature, purpose, design and relationship with investors) instead of an approach that mandates satisfaction of finite criteria outlined in paragraph 946-10-15-2 to make such a determination. Additionally, we believe that too much emphasis has been placed on ownership interest,

whereas ownership interest does not equate to control in an investment company structure as it does in a traditional corporate entity. We continue to believe that consolidation of investment companies will not yield increased transparency or enhanced financial statement reporting to users of those financial statements than currently exists. Rather, we support recognizing investment companies' pro-rata investment in investment companies at its net asset value calculated in accordance with the accounting provisions of the current ASC 946 with clear instructions on where to obtain additional financial information of investees. We believe that this is a more relevant and effective presentation for the financial statement users and would eliminate the distortion of including noncontrolling interest holdings if investment companies are consolidated.

Definition of an Investment Company

Nature of the investment activities – multiple investments

Under the Proposed ASU, an investment company must hold multiple investments. While most investment companies hold multiple investments, certain investment companies hold only one investment. One such instance is company stock funds, where employee ownership in employer stock will be held in an investment company, and employees will own units or shares of beneficial interest of the entity as part of their defined contribution retirement accounts and/or defined benefit pension plans' assets.

While the multiple investment requirement appears aimed at preventing abuse of investment company accounting by entities that do not exist to generate investment returns from capital appreciation or investment income, we believe that the requirement is too prescriptive, since it precludes entities with a legitimate business purpose of generating investment returns. We believe that the multiple investment concept should be a factor to consider when evaluating the express business purpose of the entity as part of an overall qualitative assessment of whether an entity meets the definition of an investment company.

Nature of the investment activities – returns

According to paragraph 946-10-55-7, "an entity would not meet the nature-of-the-investment-activities criterion if the entity or its affiliates obtain or have the objective of obtaining returns from its investments other than capital appreciation or investment income in entities other than an investment company or an investment property entity as defined in Topic 973." We support efforts to narrow the definition of an investment company to prevent misuse or abuse of the specialized accounting standards for investment companies; however, we believe that the example provided in paragraph 946-10-55-7(e) is too narrow in demonstrating that an entity is investing for capital appreciation or investment income, and may cause certain existing legitimate investment companies to no longer meet the investment company criteria.

Paragraph 946-10-55-7(e) indicates that an entity will not meet the nature-of-the-investment-activities criterion if the investee or its affiliates provide financing guarantees or assets to serve as collateral for borrowing arrangements of the entity or its affiliates to provide returns or with the objective of providing returns other than capital appreciation or investment income. We believe, based on this paragraph, that an entity would not meet the definition of an investment company if the entity had an investment in an investee that was the parent company of its custodian, line of credit facility provider or securities lending agent. We believe this would have a significant adverse effect on existing investment companies with investment objectives related to financial services firms, or even broad stock market indices as custodians, line of credit facility providers and securities lending agents with significant market share are included in

these broad stock market indices due to the affiliate relationships between the investee parent companies and its own various affiliated entities. We believe that this would be an unintended outcome.

Pooling of funds

The Proposed ASU indicates that entities with a single investor would not meet the investment company definition due to the pooling-of-funds criterion. Investment companies with a single or few investors are quite common in the institutional investment market. However, frequently these "single investors" actually represent multiple parties that ultimately bear the obligation to absorb losses or have the right to receive residual returns from their investment. Examples of these "single investors" include defined benefit pension plans, defined contribution retirement plans and sovereign wealth funds.

Furthermore, an institutional investor often selects an investment manager to obtain market exposure to new and/or unique market indices and sectors. Investment managers, particularly in the institutional investment market, will design investment products and/or strategies at an investors' request to meet their specialized investment goals. Investment companies are set up if the manager believes that the particular investment strategy would appeal to other investors. Accordingly, an institutional investor may be the first and only investor in an investment company for a period of several years if the investment manager does not obtain additional investors in the entity.

We recommend that a look-through provision be provided to single investors with a permitted exception to the pooling-of-funds criterion if the investment company owned by a single investor represents multiple parties at risk. This single-investor exception would be consistent to the one provided in the Board's proposal for investment property entities.¹

Consolidation

We do not believe that investment companies consolidating other investment companies in which they have a controlling financial interest will provide increased transparency or enhanced financial reporting for a number of reasons, as described below. Investment companies frequently invest in other investment companies to access an asset class or investment strategy, and thus the intent is not to seek control of the investee investment company or dictate how the investee investment company's assets will be invested. Instead, the investor investment company has determined that investment through another investment company (as opposed to direct investment in securities) represents the most efficient means to access investments with the desired exposure and return on investment. For example, an investment manager may create a fund-of-funds targeted at investors saving for retirement in a particular year. The fund-of-funds will access different asset classes through its investments in different underlying funds. The mix of underlying funds will be managed in such a way as to reduce investment risk as the retirement date approaches.

We believe that consolidation of underlying investee investment companies only provides an enhancement to existing accounting and disclosure standards in a limited number of scenarios, such as where the underlying investee investment company is wholly-owned by the investor investment company. As such, we believe that the proposed consolidation requirement should not be extended to all investment companies.

¹ Proposed Accounting Standards Update, Real Estate – Investment Property Entities (Topic 973)

We would recommend the following as a more efficient means of creating increased transparency without increasing the complexity and usability of financial statements:

- Amend U.S. GAAP to require consolidation only for an investor investment company when the
 underlying investee investment company has been created primarily for the benefit of the investor
 for taxation or regulatory purposes;
- Enhance existing financial reporting for fund-of-funds to require tabular disclosure of ownership of underlying funds; and
- Enhance transparency by requiring disclosure indicating where additional financial information about underlying investee investment companies can be found.

By providing the ownership interest and direction on where to obtain the financial information of underlying investee investment companies, we feel that the goal of increased transparency can still be achieved without significant cost to the industry.

Purpose and design of investment companies

In determining whether consolidation represents the most meaningful presentation to investors, we believe that significant consideration should be given to the purpose and design of the underlying investee investment company. If the underlying investee investment company was created primarily for the benefit of the investor investment company and to achieve a desired regulatory or tax outcome, such as a blocker funds or controlled foreign corporation, then consolidation of the underlying investee investment company would be meaningful to investors.

Fund-of-funds disclosures

A fund-of-fund structure consists of an investment company that invests in another or multiple investment companies. Many institutional investment managers utilize fund-of-funds to manage niche portfolios, such as single-country indices and fixed-income sectors, as an efficient means to manage a broader composite investment strategy. The investment manager can economically provide investment returns through managing a single investment portfolio and allow for a variety of investor bases. The fund-of-fund structure minimizes the amount of investment pools to manage, while offering a variety of investment options.

Typically, fund-of-fund structures allow for an open-ended investment portfolio construction. However, a master-feeder fund, which is a form of a fund-of-fund structure, is designed to allow multiple investor types access to a specific investment strategy. Since all types of fund-of-funds operate economically in a similar fashion, particularly in the institutional investment market, we believe that their disclosure requirements should be comparable. As such, we believe that disclosure requirements for fund-of-funds could be enhanced by extending certain aspects of master-feeder fund disclosures to all forms fund-of-funds; specifically, requiring tabular disclosure of ownership interest of investee funds and indicating where additional financial information regarding investee funds is available.

Significance of portfolio composition versus ownership interest

The investment portfolio composition of an investment company provides more meaningful information to investors than the ownership interest in the underlying investee investment companies. We are

concerned that requiring consolidation based primarily on ownership interest will lead to additional information that may not be relevant to financial statement users.

For example, a fund-of-fund may have three underlying investee funds: Fund A representing 90% of the portfolio, Fund B representing 8% of the portfolio and Fund C representing 2% of the portfolio. In this example, the fund-of-fund owns 10% of Fund A, 8% of Fund B and 85% of Fund C. Under the Proposed ASU, significant amounts of information will be required for Fund C within the fund-of-fund's consolidated financial statements, while the total return and economic performance of the fund-of-fund will be largely dictated by Fund A and B, which comprise 98% of the investment portfolio. This type of structure is common in the institutional investment market when benchmark index providers add or delete countries or market sectors from their benchmark indices.

Ownership interest affected by a number of factors

Additionally, the ownership interest of underlying investee investment companies is subject to change due to a variety of outside factors. Large institutional investors will often have significant ownership interest in a given fund. These investors will subscribe into or redeem from a given fund for a variety of factors, including a change in mandate, a rebalancing of investment portfolio and a change in overall investment strategy. One large investor subscribing into or redeeming from a given fund will significantly affect the relative ownership percentage of the other investors in the fund. Accordingly, a single investor transaction could alter the financial reporting and disclosures with respect to consolidation if the Proposed ASU is adopted as currently drafted. We believe that the accounting and disclosure requirements for investment companies should contemplate the potential for one transaction to alter the accounting and reporting outcome by placing significantly less weight on ownership interest in an investee investment company and more weight upon the power to direct activities.

Consistency in application of consolidation

Requiring consolidation of investment companies in a fund-of-fund structure is inconsistent with other accounting guidance surrounding consolidation for investment companies. Pursuant to paragraph 946-810-45-2, consolidation by an investment company of a non-investment-company is not appropriate, whereas the Proposed ASU would require consolidation of other investment companies.

An investment company is deemed to have a controlling financial interest in a non-investment-company if it holds a majority of the outstanding voting ownership interest, but the current accounting guidance does not require consolidation, as the purpose of an investment company is generally not to direct the activities of the non-investment-company, but to gain exposure to the return of the non-investment-company's voting interest's market return. The Proposed ASU would require consolidation for fund-of-funds even though an investment company generally does not have the power to direct activities, as previously noted. We believe that the accounting and disclosure requirements for investment companies should treat both investment companies and non-investment-company entities in a similar fashion, and as a matter of general practice, should not require consolidation of investments.

Failure to Qualify as an Investment Company

We believe that the application of the proposed accounting treatment discussed in paragraph 946-10-65-2 for entities that no longer meet the criteria to be investment companies could lead to a number of issues for investors, particularly those entities that fail the criteria due to the revised guidance on multiple investments and multiple investors.

These investors will still have an ownership interest in the entity; however, there will be confusion as to the nature of their investments as they have historically had interests in investment companies. This newly-designated non-investment company may not be permissible within the investors' guidelines as many institutional investors only permit investments through external investment managers via investment company ownership. These investors may then have to dispose of their previously-classified investment companies.

The most significant change for those entities that no longer meet the criteria to be investment companies will be diluted financial reporting. Investors in investment companies rely on key disclosures required under ASC 946 in order to both measure performance of the entity and to gain additional insight into the entity's investment portfolio composition. Investors utilize total return and net investment income and expense ratios to assess the economic performance and the operating efficiency of the entity. Investors also analyze the detailed investment portfolio to gain an understanding of how the entity achieves it performance, as well as the potential risks of the entity. If an entity is no longer accounted for under the existing ASC 946, this information may be omitted from the financial statements as it is not required for these newly-designated non-investment company entities, and therefore lead to diminished financial reporting for the investor.

Operational Impact

We believe that the costs of implementing the Proposed ASU would significantly outweigh any benefits achieved. The Proposed ASU would require multiple layers of consolidation for fund-of-fund structures, which will introduce numerous practical difficulties exacerbated in instances where the underlying investee investment company has a different reporting period end and is serviced at a different accounting agent. The results of these operational difficulties will increase costs for funds that will ultimately be borne by investors through increased service fees.

The open-ended nature of investment companies will require constant monitoring to assess the relative ownership percentage upon each investor transaction. Also, the open-ended nature of investment companies could lead to a fund-of-fund consolidating certain investee investment companies at period end and not consolidating the following period end due to investor transactions (subscriptions or redemptions) or vice versa. We believe that this will increase investor confusion and diminish the importance of financial reporting for fund-of-funds.

Noncontrolling Interest and Calculation of the Financial Highlights

We agree that amounts attributable to noncontrolling interests should be excluded from the calculation of financial highlights to ensure that the financial highlights present meaningful information to investors. However, we believe that the exclusion from the financial highlights illustrates why consolidating other investment companies in which a controlling financial interest is held generally does not provide meaningful information to investors. These noncontrolling interests need to be excluded from the

financial highlights, as they generally have no relationship to the investment company's interest in the other investment companies. Accordingly, these noncontrolling interest amounts should not be included within the investment company's Statement of Assets and Liabilities (Balance Sheet) or Statement of Operations (Income Statement).

Effective Date

We believe that implementing the Proposed ASU will take at least 12 to 18 months from issuance. We believe this time period would include identification and review of the amended investment company criteria for each investment company product offered and the related implementation, including working with clients to assess their new reporting requirements and addressing financial reporting for funds-offunds and entities that no longer qualify as investment companies. The Proposed ASU should prohibit early adoption in order to better ensure comparability of financial reporting.

Conclusion

We support the Board's goal of seeking a single set of high-quality, international accounting standards that companies worldwide would use for both domestic and cross-border financial reporting, and its collaborative efforts with the IASB. We support the IASB's proposal that an investment company would account for a controlling financial interest in another investment company entity at fair value,² which differs from the Board's proposed guidance. We urge the Board to continue its efforts toward convergence and appreciate your consideration of our points above prior to issue of the final standard.

Sincerely,

James J. Malerba

Executive Vice President and Corporate Controller

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² Exposure Draft, *Investment Entities*