November 30, 2007

Mr. Russell G. Golden
Director of Technical Application and Implementation Activities
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

File Reference: FSP SOP 94-3-a and AAG HCO-a
Re: Proposed FASB Staff Position SOP 94-3-a and AAG HCO-a, “Omnibus Changes to Consolidation and Equity Method Guidance for Not-for-Profit Organizations”

Dear Mr. Golden:

Deloitte & Touche LLP is pleased to comment on proposed FASB Staff Position (FSP) SOP 94-3-a and AAG HCO-a, “Omnibus Changes to Consolidation and Equity Method Guidance for Not-for-Profit Organizations” (the “proposed FSP”).

The proposed FSP further conforms the accounting of not-for-profit organizations and business enterprises; helps clarify what consolidation and equity method guidance applies to not-for-profit organizations, including health care organizations; and addresses differences in the ways these organizations apply consolidation and equity method standards and principles. We support the issuance of the proposed FSP as a final Staff Position but suggest modifications to its proposed consolidation model and transition provisions. We explain the basis for our view and our recommendations in the following paragraphs. The appendix to this letter contains additional editorial suggestions for the proposed FSP.

Consolidation Model

We support the Board’s initiative to make the consolidation guidance applicable to not-for-profit organizations in SOP 94-3\(^1\) and the Health Care Guide\(^2\) more consistent with the consolidation guidance applicable to business enterprises in ARB 51\(^3\) (as amended by Statement 94\(^4\)). As part of this project, the Board should consider eliminating the election to consolidation that currently exists in paragraph 12 of SOP 94-3 and paragraph 11.12 of the Health Care Guide and require consolidation whenever control exists regardless of its form. SOP 94-3 and the Health Care Guide currently permit, but do not require, a reporting organization within their scopes to consolidate a separate organization when control exists through a form other than ownership of a majority voting interest in another entity (e.g., a contract or affiliation agreement), if control is coupled with an economic interest.

\(^1\) AICPA Statement of Position 94-3, Reporting of Related Entities by Not-for-Profit Organizations.
\(^2\) AICPA Audit and Accounting Guide, Health Care Organizations.
\(^3\) Accounting Research Bulletin No. 51, Consolidated Financial Statements.
\(^4\) FASB Statement No. 94, Consolidation of All Majority-Owned Subsidiaries — an amendment of ARB No. 51, with related amendments of APB Opinion No. 18 and ARB No. 43, Chapter 12.
By eliminating this election to consolidate a separate not-for-profit organization, the Board would make the consolidation guidance in SOP 94-3 and the Health Care Guide more consistent with the FASB's basis for requiring the presentation of consolidated financial statements when a parent company controls a subsidiary via ownership of a majority voting interest or through means other than a majority ownership or voting interest, as discussed in ARB 51, Opinion 18,5 and Issues 97-2,6 90-15,7 96-21,5 and 97-1.9

Paragraph 1 of ARB 51 states, in part, "The purpose of consolidated financial statements is to present, primarily for the benefit of shareholders and creditors of the parent company, the results of operations and the financial position of a parent company and its subsidiaries essentially as if the group were a single company . . . ." [Emphasis added] Further, the FASB defines subsidiary in paragraph 3(c) of Opinion 18 as a corporation which is controlled, directly or indirectly, by another corporation. The usual condition for control is ownership of a majority (over 50%) of the outstanding voting stock. The power to control may exist with a lesser percentage of ownership, for example, by contract, lessee, agreement with other stockholders or by court decree. [Emphasis added] Consolidation of a separate entity by a not-for-profit entity should be required whenever control exists, regardless of whether control is in the form of ownership of a majority voting interest or through other means.

We recommend that the FASB consider a limited-scope project to comprehensively address the consolidation principles that not-for-profit organizations should follow in determining whether consolidation is appropriate when the usual characteristics of a controlling financial interest are not present, such as may be the case in special-purpose entities. It may not be appropriate to include not-for-profit organizations within the scope of Interpretation 46(R),10 a consolidation model that considers residual benefits (e.g., economic risks and rewards) when control is not present through ownership or a voting interest. However, the FASB should consider whether the guidance in Issues 90-15, 96-21, and 97-1 is adequate for identifying when consolidation is appropriate by a not-for-profit organization that is not within the scope of Interpretation 46(R), since the concepts in these Issues are outdated and applicable only to a limited number of transactions. The inability of Issues 90-15, 96-21, and 97-1 to effectively identify when consolidation is appropriate when an entity does not have ownership of a majority voting interest is supported by the FASB's extensive reconsideration of these concepts in Interpretation 46(R).

Transition

We agree with the FSP's proposed retrospective application for the provisions in paragraphs 8, 9, and 13 and prospective application for the provisions in paragraph 7.

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5 APB Opinion No. 18, The Equity Method of Accounting for Investments in Common Stock.
6 EITF Issue No. 97-2, "Application of FASB Statement No. 94 and APB Opinion No. 16 to Physician Practice Management Entities and Certain Other Entities With Contractual Management Arrangements."
7 EITF Issue No. 90-15, "Impact of Nonsubstantive Lessors, Residual Value Guarantees, and Other Provisions in Leasing Transactions."
8 EITF Issue No. 96-21, "Implementation Issues in Accounting for Leasing Transactions Involving Special-Purpose Entities."
9 EITF Issue No. 97-1, "Implementation Issues in Accounting for Lease Transactions, Including Those Involving Special-Purpose Entities."
10 FASB Interpretation No. 46(R), Consolidation of Variable Interest Entities — an interpretation of ARB No. 51.
We believe that paragraph 16 of the proposed FSP should be applied prospectively. We agree that retrospective application of the provisions in the proposed FSP would, in many cases, result in more comparable financial statements. We believe, however, that the FASB should consider whether organizations within the scope of the proposed FSP will have access to reliable and accurate information and to the resources necessary to apply the provisions in paragraph 16 retrospectively.

While Opinion 18 requires that the equity method be applied retrospectively when an investor attains significant influence over an investee, in many cases organizations will not have significant influence over the investments that will require equity method accounting pursuant to paragraph 16 of the proposed FSP. Given the nature of the investments that will require equity method accounting pursuant to the FSP (e.g., equity securities without readily determinable fair value, partnership interests, oil and gas interests, hedge funds, private equity funds, fund of funds), we believe that organizations will have difficulty contractually and logistically obtaining reliable, auditable information to record and disclose their investments retrospectively. When an organization does not exercise significant influence with respect to a nonpublic investee, it may not be able to obtain the necessary information to apply the equity method retrospectively. In addition, the investee may not have been subject to an audit, raising concerns about the reliability and accuracy of financial information associated with these investments. An organization may also have disposed of investments that would be subject to the scope of paragraph 16 and, therefore, may find it difficult to obtain timely and accurate information to account for, and prepare disclosures for, these historical investments retrospectively.

The above factors could result in an increase in the issuance of audit reports with scope limitations because of the inability of the organization's audit firm to perform adequate audit procedures in its audit of the investments.

Prospective application of paragraph 16 of the proposed FSP will give organizations the opportunity to negotiate access to the required information and to establish controls and procedures to ensure that the information used to record and disclose these investments is reliable and accurate. If the Board does require retrospective application, we recommend limiting retrospective application to those investments outstanding as of the date of adoption, thus easing the burden on preparers and auditors.

**Disclosure Requirements Related to the Equity Method of Accounting**

The FASB should consider amending the FSP to provide a scope exception to the disclosure requirements under paragraph 20 of Opinion 18 for investments in which the investee is determined not to be a not-for-profit organization as defined in paragraph 168 of Statement 117 and paragraph 6 of Concepts Statement 4. The current disclosure requirements in paragraph 20 of Opinion 18 focus on investments in common stock of corporations over which the investor has significant influence. Paragraph 20(d) of Opinion 18 requires investors to provide disclosures about these investments that include summarized information about the assets, liabilities, and results of operations of the investee.

Many investments that will require equity method accounting pursuant to the proposed FSP are not aligned with the operations or mission of the organizations affected and do not represent

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11 FASB Statement No. 117, *Financial Statements of Not-for-Profit Organizations.*
investments in the common stock of corporations. In addition, in many cases the investor organizations may not exercise significant influence over the investee. Rather, investments that will require equity method accounting pursuant to the proposed FSP could include securities without readily determinable fair values, hedge funds, mutual funds, private equity funds, and fund of funds. In these cases, disclosures regarding the assets, liabilities, and results of operations of the investee are less relevant to financial statement users than disclosures that contain the information necessary to assess the risks associated with individual investments and the portfolio of investments owned by the organization and that enable the reader to understand the characteristics and governance provisions associated with the investment. In addition, the information required to make complete disclosures under paragraph 20 of Opinion 18 may be difficult to obtain and could be unreliable if not publicly disclosed or subject to audit.

As a result, the FASB should consider amending the FSP to include disclosure requirements that are relevant to the types of investments that will require equity method accounting pursuant to the proposed FSP (e.g., those not associated with the operations or mission of the organization). Relevant disclosure for these types of investments would provide financial statement users with the information to clearly and concisely assess the risk associated with individual investments and the overall investment portfolio, in a manner similar to the disclosures required in paragraph 5(d) of Statement 132(R) for benefit plan assets. Disclosures should include information about each major category of assets and about each investment, including (1) a description of the investment, (2) the size of the investment, (3) the organization's percentage ownership interest, (4) significant governance characteristics of the investment (e.g., redemption provisions, notification periods), and (5) other information useful for understanding risks associated with the investment.

We appreciate the opportunity to comment on the proposed FSP. If you have any questions concerning our comments, please contact Robin Kramer at (203) 761-3079.

Yours truly,

Deloitte & Touche LLP

cc: Robert Uhl
    James A. Johnson

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\(^{13}\) FASB Statement No. 132(R), *Employers’ Disclosures About Pensions and Other Postretirement Benefits* — an amendment of FASB Statements No. 87, 88, and 106.
APPENDIX
Deloitte & Touche LLP
Editorial Suggestions

Paragraph 10:

We believe that it would be clearer to include the table in paragraph 10 as an appendix to the proposed FSP.

Paragraph 13:

The Board should consider revising the language in paragraph 13 as follows (added text is underlined and deleted text is struck out):

Except for the rare instances in which the provision in paragraph 4(a) are not met and of Interpretation 46(R) is applicable applies to them, not-for-profit organizations shall apply the guidance in Issue 90-15, 96-21, and 97-1 whenever they are the lessees in transactions involving SPE lessors.