Ms. Susan M. Cosper
Technical Director
File Reference No. 2016-260
Financial Accounting Standards Board
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25 July 2016

Proposed Accounting Standards Update, Consolidation (Topic 810):
Interests Held through Related Parties That Are under Common Control
(File Reference No. 2016-260)

Dear Ms. Cosper:

We appreciate the opportunity to comment on the Proposed Accounting Standards Update (ASU), Consolidation (Topic 810): Interests Held through Related Parties That Are under Common Control, issued by the Financial Accounting Standards Board (FASB or Board).

We support the FASB’s objective to change how a single decision maker or service provider should consider indirect interests when applying the consolidation guidance on determining whether it is the primary beneficiary of a variable interest entity (VIE) under the VIE model. However, we have concerns about the clarity of the VIE model, particularly the primary beneficiary guidance, when the evaluation includes entities under common control. We discuss those concerns in the appendix to this letter.

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We would be pleased to discuss our comments with the Board or its staff at your convenience.

Very truly yours,

Ernst & Young LLP
Appendix – Responses to specific questions raised in the Proposed ASU, Consolidation (Topic 810):
Interests Held through Related Parties That Are under Common Control

**Question 1:** If a reporting entity is the single decision maker of a VIE, the amendments in this proposed Update would require that reporting entity to include all of its direct variable interests in a VIE and, on a proportionate basis, its indirect variable interests in a VIE held through related parties to determine whether it is the primary beneficiary of that VIE. This evaluation would include all related parties as defined in paragraph 810-10-25-43, including those under common control with the single decision maker. Do you agree with this approach? If not, please explain why.

We agree that when a reporting entity is determining whether it is the primary beneficiary of a VIE, it should include all of its direct variable interests in the VIE and, on a proportionate basis, its indirect variable interests in the VIE.

**Question 2:** Would the proposed amendments adequately address stakeholders’ concerns that, in certain situations involving entities under common control, the amendments in Update 2015-02 may require a single decision maker of a VIE to consolidate that VIE even if it has little to no direct variable interests in the VIE?

In general we believe that the proposed amendments would address concerns that, in certain situations involving entities under common control, a single decision maker would be required to consolidate a VIE even if it doesn’t have the obligation to absorb losses of the VIE that could potentially be significant to the VIE or the right to receive benefits from the VIE that could potentially be significant to the VIE.

However, we believe that the VIE model is not clear about how to determine the primary beneficiary when the decision maker and its related parties are under common control, and as a group, appear to have the characteristics of a primary beneficiary, but the decision maker makes decisions through a fee arrangement that is not a variable interest (under paragraph 810-10-55-37).

For example, assume a manager is the single decision maker of a VIE through a fee arrangement that was deemed customary and commensurate with the services provided. The manager has a 1% equity interest in the VIE, and a related party of the manager holds a 25% investment in the VIE. The manager determines that its fee is not a variable interest based on paragraph 810-10-55-37. The manager and the related party are wholly owned subsidiaries of the same parent. Based on the primary beneficiary guidance in paragraph 810-10-25-44 through 44A, the single decision maker and its related parties under common control do not have the characteristics of a primary beneficiary because they do not have power through a variable interest (since the fee arrangement is the instrument that gives decision-making power but is not a variable interest). Therefore, if the VIE model were applied “bottoms up” as is done typically in practice, where only parties that have direct variable interests are included in the related party group when determining the primary beneficiary, no party within the related party group would consolidate the VIE.
However, we believe that the parent should ultimately consolidate the VIE because it has (1) the power to direct activities of a VIE that most significantly affect the VIE’s economic performance and (2) the obligation to absorb losses of the VIE that could potentially be significant to the VIE or the right to receive benefits from the VIE that could potentially be significant to the VIE. While we believe that this is the intended outcome of the FASB staff, we do not believe that a literal application of the VIE model is clear that the parent consolidates the VIE. We believe that changes are needed to clarify that the parent should consolidate the VIE.

ASU 2015-02 introduced the concept of an “indirect” interest when evaluating interests held by related parties. Further, paragraph 810-10-55-37D states, “indirect interests held through parties that are under common control with the decision maker should be considered the equivalent of direct interests in their entirety.” We have concerns about the interpretation of guidance on how a decision maker or service provider should evaluate other interests when the decision maker or service provider does not have an ownership interest in the related party under common control that has an investment in the VIE. The Securities and Exchange Commission (SEC) staff stated in a December 2015 speech¹ that a decision maker or service provider would not include such interests when considering the significance of the interests held by related parties under common control in the determination of whether a fee is a variable interest, unless the structure was designed to avoid consolidation by the decision maker or service provider.

We believe the Board should clarify the application of the indirect interest guidance if the proposed amendments are finalized. If the Board believes that the SEC staff interpretation remains applicable, we recommend that the Board clarifies this interpretation in the Codification so that all constituents will apply the guidance consistently. If the SEC staff interpretation would no longer be relevant, we believe that the Board should clearly articulate how to apply the indirect interest guidance in paragraph 810-10-55-37D to transactions involving a related party group under common control.

**Question 3:** Do you agree with the proposed transition requirements in paragraph 810-10-65-8? If not, what transition approach would be more appropriate?

Yes, we agree with the proposed transition requirements in paragraph 810-10-65-8.

**Question 4:** Should a reporting entity be required to provide the transition disclosures specified in this proposed Update? Should any other disclosures be required? If so, please explain why.

Yes, we believe a reporting entity should be required to provide the transition disclosures specified in paragraph 810-10-65-8m of the proposed amendments.

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¹ Comments by Christopher D. Semesky, Professional Accounting Fellow, at the 2015 AICPA National Conference on Current SEC and PCAOB Developments.
**Question 5:** Should the proposed amendments be effective immediately upon issuance of a final Update for all entities that already have adopted the amendments in Update 2015-02?

Yes, we believe the proposed amendments should be effective immediately upon issuance of a final ASU for all entities that already have adopted the amendments in ASU 2015-02.

**Question 6:** Should entities that have not yet adopted the amendments in Update 2015-02 be required to adopt the amendments in this proposed Update at the same time they adopt the amendments in Update 2015-02?

Yes, we believe that entities that have not yet adopted the amendments in ASU 2015-02 should be required to adopt the amendments in this proposed ASU at the same time they adopt the amendments in ASU 2015-02.