February 14, 2012

Technical Director
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Re: Proposed Accounting Standards Update, Consolidation (Topic 810): Principal versus Agent Analysis

Dear Technical Director:

On behalf of the Securities Industry and Financial Markets Association Asset Management Group (the “AMG”) Accounting Committee, we appreciate the opportunity to provide comments on the FASB’s Proposed Accounting Standards Update, Consolidation (Topic 810): Principal versus Agent Analysis (the “Proposed Update”).

The AMG’s members represent U.S. asset management firms whose combined assets under management exceed $20 trillion. The AMG Accounting Committee includes many of the industry’s major independent asset management firms along with banks and insurance companies with significant asset management businesses. The individuals who serve on the AMG Accounting Committee are senior accounting policy professionals at their respective firms.

We commend the Board in its efforts to develop a framework for determining whether a decision maker should consolidate an entity based upon whether it is acting in a principal or agency capacity. We appreciate that the Board understood and acknowledged the concerns of the asset management industry by granting a deferral under ASU No. 2010-10 from the provisions of ASC 810 (codification of FAS 167) for reporting entities with interests in investment companies.

We support the Board’s separate efforts to clarify the definition of an investment company. We continue to believe that the consolidation of investment companies will not yield meaningful financial statement reporting to the users of those financial statements. Once a final definition for an investment company is determined, we support recognizing asset managers’ pro-rata investments in investment companies at their net asset values calculated in accordance with the accounting provisions of ASC 946, rather than consolidation of such investment companies by asset managers. We believe that this is a more relevant presentation for the users of the asset managers’ financial statements and would eliminate the distortion of including minority interest holdings if investment companies are consolidated.

The balance of our letter specifically addresses our responses to certain questions identified in the Proposed Update and other comments.
**Question 1:** When determining whether a decision maker is a principal or an agent, the proposed amendments require the analysis to consider the decision maker's overall relationship with the entity and the other parties involved with the entity. This analysis would be based on a qualitative assessment. Do you agree with this approach? If not, why?

In a consolidation model based on control, the principal versus agent determination is a critical component for any entity in a service-based industry such as ours. We are supportive of a qualitative approach for determining whether a decision maker is acting as a principal or an agent.

**Question 2:** The evaluation of a decision maker's capacity would consider the following factors:

a. The rights held by other parties
b. The compensation to which the decision maker is entitled in accordance with its compensation agreement(s)
c. The decision maker's exposure to variability of returns from other interests that it holds in the entity.

Are the proposed factors for assessing whether a decision maker is a principal or an agent appropriate and operational? If not, why? Are there any other factors that the Board should consider including in this analysis?

In addition to the proposed factors, we recommend “the purpose and design of the entity” be another factor to consider in the analysis. Paragraph ASC 810-10-25-39C states: “This assessment also shall consider the entity’s purpose and design, including the risks that the entity was designed to create and pass through to its interest holders.” We interpret this to mean that the Board’s intent is for the purpose and design of the entity to be considered along with the other factors. We are concerned that by not making it a specific factor to consider in the evaluation of a decision maker’s capacity, some may interpret the language to suggest that it is not of equal importance in the principal versus agent assessment.

We agree that the proposed factors should be considered in assessing whether a decision maker is a principal or an agent. We are concerned that the overemphasis given to the consideration of proposed factor c. in the examples provided in the Proposed Update will result in the emergence of bright lines for asset managers; this concern is articulated in our response to Question 3 below.

We also believe the existence of an independent board of trustees/directors should be a determinative factor considered in the determination of principal versus agent. More specifically, a board governed by the Investment Company Act of 1940 (“1940 Act”) in the United States should be a determinative indicator that the asset manager is acting as an agent. This view is discussed in more detail in our response to Question 4 below.

**Question 3:** The proposed Update would require judgment in determining how to weigh each factor in the overall principal versus agent analysis. Do you agree that the proposed amendments, including the related implementation guidance and illustrative examples, will result in consistent conclusions? If not, what changes do you recommend?

In a model that requires a qualitative assessment with the weighting of factors, the presence of an overarching accounting principle that considers the purpose and design of the entity is critical to create a standard that will produce consistent accounting conclusions. The Proposed Update requires that the level
of equity interest be considered in the determination of principal versus agent, and suggests that the
greater the equity interest, the more weight that factor should carry. We believe that the level of equity
interest is only one factor to consider in evaluating whether a decision maker is acting as an agent or a
principal. We believe that this factor needs to be evaluated in the context of all of the factors taken
together, including the overall purpose and design of the entity.

The purpose and design of the entity is extremely important in understanding why a decision maker is
holding an equity interest (i.e., to align its interests with the entity investors versus to give the decision
maker significant exposure to the investment objectives of the entity for its own proprietary risk taking).
We agree that the level of equity interest should be considered for purposes of determining control. We
disagree, however, that the extent of a decision maker's equity involvement should be determinative.

Asset managers are required by fiduciary duty to make decisions in the best interest of the investors of the
fund. This fiduciary duty is not affected by the existence of an investment in the fund by the asset
manager, regardless of the size of the investment. Allowing our equity investment in the fund to alter our
investment decisions violates fiduciary law. Regulations under the 1940 Act and other applicable laws are
devised to mitigate any apparent conflicts of interest including conflicts which may arise as a result of
holding investments in the fund. Therefore, we do not support a model that suggests that these decisions
differ solely depending on the extent of our holdings in the fund.

**Question 4:** Should substantive kick-out and participating rights held by multiple unrelated parties be
considered when evaluating whether a reporting entity should consolidate another entity? If so, do you
agree that when those rights are held by multiple unrelated parties, they should not in and of themselves
be determinative? If not, why? Are the guidance and implementation examples illustrating how a
reporting entity should consider rights held by multiple unrelated parties in its analysis sufficiently clear
and operational?

We agree that substantive kick-out and participating rights should be considered when evaluating whether
a reporting entity should consolidate another entity. Whether these rights are held by a single or multiple
unrelated parties, they should be considered in the principal versus agent analysis when they are deemed
**substantive.** The number and/or dispersion of unrelated parties that collectively need to exercise these
rights should be considered in the evaluation of whether the rights are **substantive.** However, once the
rights are deemed **substantive** they should be determinative in concluding that the decision maker is
acting in an agent capacity.

As noted above, we believe an independent board meeting certain criteria should be a determinative
indicator that the asset manager is acting as agent. Certain types of funds (e.g., those regulated under the
1940 Act) are required to have a board, acting as a single unit, with the full power and authority to carry
out all actions necessary and appropriate in connection with the management of an investment fund,
including decisions regarding all service providers, fee structures, the introduction of new share classes,
the declaration of dividends, and distributions of income and capital gains, etc. The board should also have
the ability to terminate the asset management contract without cause. The rules and regulations governing
the purpose and design of funds with boards meeting these criteria are just as meaningful and substantive
as a board for an operating entity. We believe the existence of such a board should be sufficient to
conclude that the investment advisor is an agent of a fund.
There is disparity between the guidance in paragraph ASC 810-10-25-41D and the Board’s belief, as noted in the basis for conclusions paragraph BCI8, that “kick-out and participation rights should affect only the consolidation analysis when there is a realistic possibility that the other interest holders may exercise those rights.” We believe that the likelihood that either kick-out or participating rights will be exercised is irrelevant to determining whether the rights themselves are substantive, consistent with the guidance in paragraph ASC 810-10-25-41D that “the likelihood that the participating rights will be exercised by the interest holder shall not be considered when assessing whether a participating right is substantive.” We encourage the Board to update the basis for conclusion provided to allow for consistent application of the fact that probability of exercise is not relevant for determining if the rights are substantive. We believe that kick-out or participating rights are not regularly exercised due to their substance because their existence incents the behavior of the decision maker to prevent the exercise of such rights.

Under prior limited partnership consolidation guidance, the general partner was presumed to control the limited partnership unless the limited partners held substantive participation or removal rights, which overcame this presumption of control. If the presumption of control by the general partner was overcome, a limited partner would only consolidate the limited partnership if it could unilaterally control the entity. We encourage the Board to provide guidance that clarifies when an investor in a limited partnership, who is unrelated to the decision maker acting in an agent capacity, would be deemed principal, and therefore consolidate the entity.

**Question 8:** The Board decided to include the principal versus agent assessment as a separate analysis within the overall consolidation assessment, rather than replacing the current guidance for evaluating whether a decision-making arrangement is a variable interest (and accordingly, a principal) with the revised principal versus agent analysis. The Board believes that if an entity’s fee arrangement does not meet the definition of a variable interest (for example, a nominal performance-based fee), the decision maker should not be required to continue the consolidation assessment. Do you agree? If not, why?

We agree that replacing the current guidance for evaluating whether a decision-making arrangement is a variable interest with the proposed principal versus agent analysis and amending the disclosure requirements would result in a more operationally efficient consolidation assessment. A decision maker must evaluate whether its rights and obligations are consistent with that of a principal or agent. Therefore, requiring an assessment of a decision maker’s remuneration as a variable interest seems redundant.

**Question 10:** Update 2010-10 was issued to address concerns that some believe that the consolidation requirements resulting from Statement 167 would have required certain funds (for example, money market funds that are required to comply with or operate in accordance with requirements that are similar to those included in Rule 2a-7 of the Investment Company Act of 1940) to be consolidated by their investment managers. The amendments in this proposed Update would rescind the indefinite deferral in Update 2010-10 and would require money market funds to be evaluated for consolidation under the revised guidance. The Board does not intend the application of the proposed Update to result in money market funds being consolidated. Do you agree that the application of the proposed Update will meet this objective? If not, why and what amendments would you recommend to address this issue?

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1 In accordance with ASC 810-10-55-37 (formerly paragraph B22 of FIN 46(R), Consolidation of Variable Interest Entities)
We believe the only modification to the Proposed Update to assure achievement of the Board’s stated intent that money market funds not be consolidated by their investment managers as a result of applying the proposed guidance is for the FASB to provide a specific exemption from consolidation for money market funds. We understand that within the proposed principal versus agent analysis, money market funds that are subject to Rule 2a-7 possess a substantive board, which could overcome the implicit or explicit financial responsibility concept in assessing principal/agent characteristics. However, this is subjective logic that may not be applied consistently and further, is not viable for money market funds not subject to Rule 2a-7 (i.e., certain international funds that operate in accordance with requirements that are similar to those included in Rule 2a-7).

Further, given the ongoing deliberations by regulators of the design and operation of money market funds, the Board should consider the potential structural changes to the money market fund type. If the intent is not to consolidate these fund types, then a blanket exception would prevent future consolidation as a result of potential regulatory changes to their structure.

**Question 11:** For purpose of applying the proposed principal versus agent guidance, the proposed amendments would require a reporting entity to include the decision maker’s direct and indirect interests held in an entity through its related parties. Do you agree with the requirement that a decision maker should include its proportionate indirect interest held through its related parties for purpose of applying the principal versus agent analysis? Why or why not?

We support the Board’s efforts to capture all of a decision maker’s direct and indirect interests held in an entity through its related parties to prevent misuse or abuse of the consolidation accounting standards. We understand the Board’s concern that decision makers could structure entities through its indirect interests in an effort to avoid consolidation and achieve an outcome that would be less transparent to the users of the financial statements.

We remain concerned with the guidance for evaluating a decision maker’s indirect interests held by employees and employee benefit plans for inclusion with the decision maker’s direct interests. In paragraph ASC 810-10-25-42, the Board stated: “Similarly, if an employee of the decision maker is a related party and owns an interest in the entity being evaluated and that employee’s interest has been financed by the decision maker, the decision maker shall include its indirect interest in the evaluation.”

We do not believe that the Board’s proposed language is clear, and suggest the Board clarify what constitutes an employee’s interests financed by the decision maker. In addition, there is no reference to treatment of interests held by employee benefit plans. We believe that there are legitimate reasons when employees and employee benefit plans, such as participant-directed 401(k) plans, invest in investment fund entities. We suggest that the Board retain the proposed deleted exclusions from related parties in ASC 810-10-55-37A subparagraphs a and b, specifically excluding interests of employees and employee benefit plans of the decision maker except if they are used in an effort to circumvent the provisions of the proposed principal versus agent guidance.

When evaluating related parties under ASC 850, certain employees of an investment manager meet the related party definition, including owners or partial owners and management of the entity. Employees of investment managers often invest at their own discretion using their funds (i.e., not deferred compensation) and at their own risk in investment management products managed by their firm. These
discretionary investments may be made in retirement pre-tax products, such as participant-directed 401(k) plans, certain vested deferred compensation plans and taxable products such as registered investment funds. In these situations, the firm has no economic exposure to the employee investments and vice versa and these employee investments should not be included in the indirect interests of the decision maker.

**Question 13:** Do you agree with the proposed transition requirements in paragraph 810-10-65-4? If not, how would you propose to amend those requirements, and why? Please provide an estimate of how long it would reasonably take to implement the proposed requirements.

We believe the Proposed Update should be effective at the beginning of the first calendar year at least one year after the standard has been issued. Implementation of the Proposed Update will require a detailed, comprehensive assessment of an entity’s relationship with VIEs and limited partnerships. This will necessitate a significant amount of evaluation and analysis by the entity, particularly for an asset manager as a result of the large number of investment funds it manages, as the concepts are generally complex and requires thoughtful analysis. Nevertheless, we believe that early adoption should be permitted.

**Question 14:** Should early adoption be permitted? If not, why?

We support an option for early adoption for those entities that wish to do so.

**Other Comments: Definition of Terms**

The terms “variability of returns”, “anticipated economic performance” and “maximum exposure to loss” are used throughout the Proposed Update. Because these terms are related to similar, although different, measures of an entity’s economic performance, we suggest providing definitions in the Master Glossary to help avoid confusion between these terms and ensure consistency in interpretation and application of the guidance. We have provided definitions of the terms as we understand them below:

**Variability of returns** is a measure of the extent to which the returns on an investment or of fees paid to a service provider may fluctuate based on the different possible outcomes for the economic performance of the entity. Variability of returns includes both upside and downside (i.e., returns that are greater and returns that are less than the mean return).

**Anticipated economic performance** represents the expected possible outcomes related to a measure of the economic performance of the entity. For example, available cash flow may be one such measure of economic performance.

**Maximum exposure to loss** is a measure of the largest possible principal loss that an investor contractually may suffer. Examples include the total loss of principal of an investment and a loss on a guarantee equal to the full notional amount of the guarantee. Maximum exposure to loss does not include the failure to receive an upside return. For example, the failure to receive a fee is not included in maximum exposure to loss.

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We appreciate your consideration of these matters and welcome the opportunity to discuss them with you.

Sincerely,

Sean P. Newth  
Chairman  
SIFMA Asset Management Group Accounting Committee  

cc: Michael Stewart, Director of Implementation Activities, International Accounting Standards Board  
cc: Timothy W. Cameron, Esq., Managing Director, SIFMA Asset Management Group  
cc: Mary Kay Scucci, PhD., CPA, Managing Director, U.S. Business Policy and Practices  
cc: SIFMA Asset Management Group Accounting Committee