December 10, 2012

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

Re: File Reference No. EITF 12-G, Consolidation (Topic 810), Accounting for the Difference Between the Fair Value of the Assets and the Fair Value of the Liabilities of a Consolidated Financing Entity

Dear Technical Director:

MassMutual Financial Group\(^1\) appreciates the opportunity to submit this letter in response to the request for comment by the Financial Accounting Standards Board ("Board") regarding the Exposure Draft of Proposed Accounting Standards Update (ASU), "Consolidation (Topic 810): Accounting for the Difference between the Fair Value of the Assets and the Fair Value of the Liabilities of a Consolidated Collateralized Financing Entity (a consensus of the FASB Emerging Issues Task Force)." We agree with the Board’s efforts to develop accounting guidance that would resolve the diversity in practice in the accounting for the difference between the fair value of the financial assets and the fair value of the financial liabilities of a consolidated collateralized financing entity (CFE) and to arrive at the amount a reporting entity would ultimately expect to realize. However, in addition to our responses to the Board’s questions for respondents, which are attached in an Appendix to this letter, we would like to share the following observations and comments on aspects of the proposed guidance.

**Definition of Collateralized Financing Entity**

The proposed ASU amends the Accounting Standards Codification (ASC) Master Glossary to define a collateralized financing entity as:

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\(^1\) MassMutual Financial Group is a marketing name for Massachusetts Mutual Life Insurance Company (MassMutual) and its affiliated companies and sales representatives. MassMutual is headquartered in Springfield, Massachusetts and its major affiliates include: Babson Capital Management LLC; Baring Asset Management Limited; Cornerstone Real Estate Advisers LLC; The First Mercantile Trust Company; MassMutual International LLC; MML Investors Services, LLC; Member FINRA and SIPC; OppenheimerFunds, Inc.; and The MassMutual Trust Company, FSB.
A variable interest entity that holds debt instruments, issues beneficial interests in those financial assets, and has no equity. All the beneficial interests are financial liabilities that only have recourse to the related financial assets of the collateralized financing entity.

We believe the requirement to have no equity, if taken literally, is too restrictive. In most instances, CFEs are established with some minor, non-participating equity interests that are held by a party other than the primary beneficiary. Therefore, we suggest that the definition be refined to say “nominal equity” or something similar to more accurately reflect the typical structure of CFEs.

Interaction of Proposed Guidance with Other Ongoing Projects

As noted above, we welcome the Board’s efforts to resolve diversity in practice on this subject. However, it is not clear how this proposed guidance may be impacted by the Board’s ongoing projects related to Investment Companies and Consolidation. As the Board redeliberates this proposed guidance, we ask that it consider whether this issue would be better addressed as part of those projects or align the effective date of this proposed ASU with those projects in order to avoid any unintended consequences or causing companies to potentially modify the accounting for this topic twice. For example, if adopted by the Board, under the proposed principal versus agent consolidations guidance\(^2\), a reporting entity may be able to deconsolidate CFEs. It would be costly and inefficient to restate historical financial statement to comply with this proposed ASU only to subsequently deconsolidate the CFE upon the issuance of the final consolidations guidance.

Our responses to the Board’s specific questions are set forth in the following Appendix. If you have any questions about our comments or wish to discuss any of the matters addressed herein, please feel free to contact us. We would be pleased to discuss our comments further with the FASB staff.

Sincerely,

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\(^2\) Proposed Accounting Standards Update - Consolidation (Topic B10): Principal versus Agent Analysis

Massachusetts Mutual Life Insurance Company and affiliated companies   Springfield MA 01111-0001
Appendix

**Question 1:** Do you agree that a reporting entity should measure the fair value of a collateralized financing entity’s financial assets and financial liabilities consistently with how market participants would price the reporting entity’s net risk exposure (that is, how a market participant measures the retained beneficial interest held by the reporting entity) at the measurement date?

We believe that the fair value of a CFE’s assets and liabilities should be measured in a manner consistent with the rights and obligations associated with those assets and liabilities. That is, if the assets of the CFE are only available to satisfy the liabilities of the CFE, and the liability holders (beneficial interest) have no recourse other than to the CFE’s assets, the liabilities should be measured at an amount equal to the assets available to satisfy them.

Based on paragraph BC7 of the proposed ASU, we believe it is the Board’s intention that the proposed guidance will allow CFEs within its scope to apply the measurement guidance in paragraph 820-10-35-18D. In order to do that, the requirement in paragraph 820-10-35-18E(c) must be met (that is, the reporting entity measures the financial assets and financial liabilities at fair value). However, it is not clear if when adopting the proposed guidance a reporting entity would be provided an opportunity to elect the fair value option. If that is the Board’s intention, we believe it should be made more explicit before finalizing the proposed ASU. If reporting entities are not allowed to elect to the fair value option when adopting the proposed ASU, the noted diversity in practice may not be eliminated.

**Question 2:** Do you agree that the scope of the amendments in this proposed Update should apply to all entities that are required to consolidate a collateralized financing entity, as defined, and are required to or have elected, under Topic 825, to measure all eligible financial assets and financial liabilities of the collateralized financing entity at fair value?

No. We do not understand how the election of the fair value option (FVO) should change the accounting for the underlying economics of an entity. If the beneficial interest holders only have recourse to the CFE’s assets, the CFE’s economic structure is unchanged by the election of the FVO. Therefore, any change in the value of the CFE’s assets is to the economic benefit or detriment of the beneficial interest holders to the extent of their investment regardless of whether the CFE carries those beneficial interests at fair value or amortized cost. Likewise, the attribution of these economics should be to the party that will eventually absorb them.

Also, by not applying this to CFEs for which the FVO was not elected would retain diversity in practice in accounting for CFEs. This diversity could happen within and among reporting entities. For example, a reporting entity could have elected the FVO for CFE(s) that it was required to initially consolidate as a result of the adoption of ASU
2009-17. That same reporting entity could also have CFE(s) for which the FVO was not elected, which would be the case if a reporting entity was required to consolidate a CFE prior to the adoption of ASU 2009-17 and was, therefore, not provided the option of electing the FVO. Similarly, the reporting entity may not have elected the FVO for a CFE that it was required to consolidate due to the adoption of ASU 2009-17.

Further, as we currently understand this proposed guidance, going forward, a reporting entity would be required to account for a CFE’s assets and liabilities at fair value upon initial recognition and subsequently at each reporting date. If this is the Board’s intent, this would potentially cause three different accounting scenarios for CFEs; CFEs that carry liabilities at amortized cost, CFEs for which the FVO was elected, and CFEs that are required to carry assets and liabilities at fair value if this guidance is adopted. To further complicate this, it is our understanding that there is also currently diversity in practice as to whether CFEs are considered investments companies. If our understanding is correct, depending on how a reporting entity classifies a CFE, it may account for the CFE’s assets at amortized cost, fair value through other comprehensive income or fair value through income. Therefore, the potential exists that many CFEs may not be within the scope of the proposed guidance and that diversity in practice would continue.

To alleviate these inconsistencies, we suggest the Board allow a reporting entity to elect the FVO for all CFEs consolidated at the adoption date of this guidance.

**Question 3:** Do you believe that current U.S. GAAP provides guidance for reporting entities about how to account for any differences between the carrying amount of the financial assets and the carrying amount of the financial liabilities of a consolidated collateralized financing entity that is not within the scope of this proposed Update? If not, please explain why.

It is our belief that economics of an entity should be attributable based on rights and obligation of the parties that will ultimately absorb them. We believe that there is current guidance for the attribution of net income or loss and net asset for all types of entities regardless of how those rights and obligations are obtained (i.e., ownership, contract). However, we believe that this guidance has been misinterpreted. Although ASC paragraph 810-10-45-16A states:

*Only either of the following can be a noncontrolling interest in the consolidated financial statements:*

a. A financial instrument (or an embedded feature) issued by a subsidiary that is classified as equity in the subsidiary’s financial statements...

The ASC Master Glossary defines a noncontrolling interest as “[t]he portion of equity (net assets) in a subsidiary not attributable, directly or indirectly, to a parent. A noncontrolling interest is sometimes called a minority interest.”

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3 ASU 2009-17, Consolidations (Topic 810): Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities (f.k.a. FASB Statement No. 167, Amendments to FASB Interpretation No. 46(R) [FAS No. 167])
Statement No. 6 paragraph 49 defined equity as “the residual interest in the assets of an entity that remains after deducting its liabilities.”

We do not believe these definitions constrain a noncontrolling interest to a financial instrument (i.e., common stock) classified as equity nor do they state that a residual interest in an entity can only be attributed to a financial instrument classified as equity of the entity. Taken together, a noncontrolling interest is the residual interest of an entity that is not attributable to the parent. However, only financial instruments classified as equity in a subsidiary can be a noncontrolling interest. Therefore, the net income or loss of subsidiary can be attributable to the investors that hold the rights or obligations to absorb an entity’s economics as a noncontrolling interest, however, if those rights and obligations are obtained through investments in an interest other than financial instruments classified as equity (i.e., beneficial interest), those interests should not be reclassified to noncontrolling interest (equity) at the parent level. However, the gains and losses associated with those rights and obligations should be segregated from the parent’s as a noncontrolling interest.

This interpretation is supported by the following passages, each of which discusses the attribution of income or loss but not associating that attribution to an ownership in a financial instrument classified as equity of the investee:

To determine the investor’s share of venture net income or loss, such agreements or arrangements shall be analyzed to determine how an increase or decrease in net assets of the venture (determined in conformity with GAAP) will affect cash payment to the investor over the life of the venture and on its liquidation. Specified profit and loss allocation ratios shall not be used to determine an investor’s equity in venture earnings if the allocation of cash distributions and liquidating distributions are determined on some other basis. [ASC ¶970-323-35-17]

The Board, therefore, decided to require that net income and comprehensive income be attributed to the parent and the noncontrolling interest but not provide detailed guidance for making the attribution. The Board observed that entities were making attributions before this Statement was issued and that those attributions generally were reasonable and appropriate. Therefore, the Board decided that detailed guidance was not needed. [FAS No. 160 ¶B38]

The interpretation of guidance that net income or loss can only be attributable to a financial instrument classified as equity by the investee is what creates the issue with the attribution of income or loss for CFEs. If guidance clearly stated that gains and losses should be attributable to those that will ultimately absorb them regardless of how those rights or obligations are obtained (i.e., contract, beneficial interest, common stock), there would not be an issue regarding the attribution of a CFE’s economics, and the issue of whether the liabilities of a CFE were carried at fair value or amortized cost would not matter.

For this reason, we recommend that the Board provide additional guidance that allows the attribution of income and net assets to owners that have rights to that income or
net assets regardless of whether those rights are obtained through the ownership of a financial instrument classified as equity or not. This attribution methodology would provide financial statement users with information that is more transparent, intuitive, informative and consistent with the legal claims the entity’s investors have to its assets. We also suggest the Board consider including this attribution guidance within the proposed consolidation guidance that is expected to be issued during the first half of 2013.

**Question 4**: Do you agree that the proposed amendments should be applied using a modified retrospective approach, with the option to apply the proposed amendments retrospectively? If not, please explain why.

Yes. We believe a modified retrospective approach, with the option to apply the proposed amendments retrospectively, is appropriate.

However, we are concerned that if this guidance is adopted prior to the new principle versus agent consolidation guidance expected to be issued during 2013, a significant amount of time and effort would be put forth by a reporting entity to comply with the transition guidance of this proposed ASU when, in fact, under the proposed consolidation guidance, some of these CFE’s would deconsolidate in the future. Therefore, we suggest combining or considering this guidance in conjunction with other proposed guidance in an effort to fix the issue once in an effective and efficient manner. As mentioned in our response to Question 3, this could be done by clarifying the definition of a noncontrolling interest and the related attribution guidance.

**Question 5**: Do you agree that early adoption of the proposed amendments should be permitted? If not, please explain why.

As there currently is diversity in practice, we do not anticipate any issue if early adoption is allowed.

**Question 6**: Is the guidance in paragraphs 820-10-35-18D and 820-10-35-18F difficult to apply to collateralized financing entities, as defined? If so, what additional information would be useful in applying the guidance in this proposed Update?

Yes. As currently defined in the proposed ASU, many structured entities (CFEs) would not meet the definition. As discussed above, there are many instances where a reporting entity may not have elected or been able to elect the FVO for a CFE’s liabilities. Therefore, the requirement in 820-10-35-18E(c) would not have been met providing a reporting entity the ability to apply the guidance of paragraphs 820-10-35-18D and 820-10-35-18F.

820-10-35-18D also states that “If the reporting entity manages that group of financial assets and financial liabilities on the basis of its net exposure to either market risks or credit risk, the reporting entity is permitted to apply an exception to this Topic for measuring fair value.” In our experience, a CFE’s net risk may not be managed on the basis of its exposure to either market risks or credit risk as the risk related to the assets and the risks related to the liabilities may involve different counterparties.
The proposed ASU does not provide guidance for the attribution of the fair value of the assets to the liabilities. For example, should the fair value of the assets be allocated to fair value of the liabilities based on contractual obligation including subordination or the relative fair value of the obligation? Different allocation methods could yield significantly different outcomes. For example, a CFE has three tranches with contractual values of $120, $80 and $50 and fair values of $120, $60 and $10, respectively, and the primary beneficiary holds the lowest tranche. If the fair value of the CFE’s assets is $200, should that value be attributable to the two upper tranches based on contractual value with the primary beneficiary recognizing a loss of $50, or should it be attributable based on the fair value of the CFE’s obligations and the primary beneficiary only recognize a $30 loss?

The proposed ASU also does not provide guidance on how to attribute an excess in the fair value of a CFE’s assets over the CFE’s contractual obligations. For example, if the CFE’s maximum contractual obligation is $200 and the fair value of the CFE’s assets is $205, if there is no remaining ownership in the form of a financial instrument classified as equity, to what party (or parties) is the $5 residual value attributable to?

We believe each of the above issues would be resolved if the Board addressed the attribution of net income or loss and net assets as discussed in our response to Question 3.

Question 7: The proposed amendments would apply to public and nonpublic entities. Should the proposed amendments be different for nonpublic entities? If so, please describe how and why you think they should be different.

No. We believe the guidance should be the same for public and nonpublic entities. Not only would this create consistency and comparability, it would limit the potential for a public entity that consolidates a private entity to create structures to achieve different accounting results.

Question 8: For preparers, how much time would be needed to implement the proposed amendments?

We believe that it could potentially take up to one year to implement this guidance.

Question 9: For preparers, what costs do you expect to incur as a result of implementing the proposed amendments?

It is difficult to estimate the cost of implementing this proposed guidance. However, the financial results and financial statement presentation would more appropriately reflect the economics of a reporting entity that is a primary beneficiary of a CFE. Therefore, we believe the benefits would be worth the costs incurred to implement the guidance.