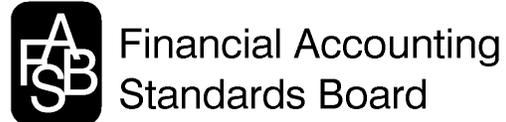


**MINUTES**



**To:** Board Members  
**From:** Interpretation 46(R) Team (Mathys, x446)  
**Subject:** Minutes of the April 1, 2009, Board Meeting: Interpretation 46(R)      **Date:** June 11, 2009  
**cc:** FASB: Golden, Bielstein, Lott, Donoghue, Lusniak, Mayer, Schonefeld, Sperry, Barker, Roberge, Hood, Chookaszian, Posta, Gabriele, Sutay, Glotzer, Klimek, C. Smith, Mechanick, Nickell, Mathys, Burnap, Cropsey, Proestakes, Wilkins, Stoklosa, FASB Intranet; IASB: Leisenring, Kusi-Yeboah, Teixeira

*The Board meeting minutes are provided for the information and convenience of constituents who want to follow the Board's deliberations. All of the conclusions reported are tentative and may be changed at future Board meetings. Decisions become final only after a formal written ballot to issue a final Statement, Interpretation, or FASB Staff Position.*

Topic: Interpretation 46(R)  
Basis for Discussion: Redeliberation of Issues  
Length of Discussion: 10:45 a.m. to 11:40 a.m.

Attendance:

Board members present: FASB: Herz, Linsmeier, Seidman, L. Smith, and Siegel  
Board members absent: None  
Staff in charge of topic: Roberge and Nickell  
Other staff at Board table: Golden, Stoklosa, C. Smith, and Mathys

## Summary of Decisions Reached

The Board continued its redeliberations of the Exposure Draft, Amendments to FASB Interpretation No. 46(R), and reached the following decisions:

1. **Disclosures.** The Board decided to retain the disclosure requirements applicable to Interpretation 46(R) within FSP FAS 140-4 and FIN 46(R)-8, *Disclosures by Public Entities (Enterprises) about Transfers of Financial Assets and Interests in Variable Interest Entities*, with only minor editorial changes. The Board also decided to add the following disclosure requirement to paragraph 24 of FASB Interpretation No. 46(R), *Consolidation of Variable Interest Entities*, for situations in which an enterprise concludes that its power is shared (subject to refinement during drafting):

If applicable, significant factors considered and judgments made in determining that power to direct the activities of a variable interest entity that most significantly impact its economic performance is shared pursuant to the guidance in paragraph 14X.

2. **Related party guidance (paragraph 16).** The Board decided to amend the criterion in paragraph 16(d)(1) of Interpretation 46(R) to provide an exemption for substantive mutual transfer restrictions based on mutually agreed upon terms by willing, independent parties.
3. **Related party guidance (paragraph 17).** The Board decided to amend paragraph 17 of the Exposure Draft to eliminate factors (c) and (e) of that paragraph. Additionally, the Board decided to explicitly emphasize in paragraph 17 that the individual parties within a related party group were required to first separately consider the consolidation guidance in paragraphs 14(a) and 14(b) of the proposed amendments before performing the existing analysis for determining which party, within a related party group, is the primary beneficiary of a variable interest entity. The Board decided to amend paragraph 17 as follows (subject to refinement during drafting):

In situations in which an enterprise concludes it does meet the criteria in paragraph 14(a) and (b) but, as a group, the enterprise and its related parties If two or more related parties (including the de facto agents described in paragraph 16) would be identified as the primary beneficiary of the entity, hold variable interests in the same variable interest entity, and the aggregate variable interest held by those parties would, if held by a single party, identify that party as the primary beneficiary, then the party within the related party group that is most closely associated with the variable interest entity is the primary beneficiary. The determination of which party within the related party group is most closely associated with the variable interest entity requires judgment and shall be based on an analysis of all relevant facts and circumstances, including:

- a. The existence of a principal-agency relationship between parties within the related party group
  - b. The relationship and significance of the activities of the variable interest entity to the various parties within the related party group
  - c. A party's exposure to the expected losses of the variable interest entity
  - d. The design of the variable interest entity.
  - e. The extent to which a party meets criteria a and b in paragraph 14A.
4. **Separate classification of elements.** The Board decided to require separate classification of elements on the face of the primary beneficiary's balance sheet for:
- a. Those assets of a consolidated variable interest entity that can only be used to settle obligations of consolidated VIEs
  - b. Those liabilities of a consolidated variable interest entity for which creditors of the consolidated VIE have no recourse to the general credit of the primary beneficiary.
5. **Other.** The Board decided to emphasize in the Introduction to the proposed amendments to Interpretation 46(R) that applying the provisions of the proposed amendments, terms, transactions, and arrangements, whether contractual or noncontractual, must (a) be substantive and (b) be representative of economic reality and (c) not used in a manner to circumvent the purpose and provisions of the Interpretation.

Objectives of Meeting:

The objective of this meeting was to discuss (a) disclosures, (b) related party guidance, and (c) separate classification of elements. The objective was met.

Matters Discussed and Decisions Reached:

**Issue 1: Disclosures**

1. Mr. Roberge noted that, through discussions with investors, the staff learned that the requirements of FSP FAS 140-4 and FIN 46(R)-8 provide useful information. Mr. Roberge stated that the staff recommends that the disclosure requirements in the final Statement be consistent with the disclosures in Interpretation 46(R), along with additional disclosure requirements about shared power.
2. **Staff Recommendation:** Mr. Roberge noted that, absent any further disclosure requests from financial statement users, the staff believes that no additional

deliberations regarding disclosures are necessary. The staff recommended retaining disclosures consistent with those applicable to Interpretation 46(R) within the FSP with only minor editorial changes, and the removal of the “significant” qualifier from paragraph 24. In addition, the staff recommends the following disclosure requirement be added to paragraph 24 of Interpretation 46(R) for situations in which an enterprise concludes that its power is shared:

If applicable, significant factors considered and judgments made in determining that power to direct the activities of a variable interest that most significantly impact its economic performance is shared pursuant to the guidance in paragraph 14X.

3. **Board Vote:** The Board unanimously agreed with the staff recommendation.
4. **Board Comments:** Mr. Siegel expressed concern with the concepts of “potential power” and “future power,” noting that he would like to see enterprises consolidate variable interest entities before losses occur and the enterprise discovers that it was, in fact, the primary beneficiary of the entity the entire time.
5. Mr. L. Smith noted that there are disclosure requirements for enterprises that hold a variable interest but are not the entity’s primary beneficiary, and those disclosure requirements could capture the instances that may require the enterprise to provide support for the entity.
6. Mr. Linsmeier noted that this is an extension of previous conversations among Board members who would like the Statement to make it clear that “power” refers to the power an enterprise has throughout the life of the entity, rather than power that exists at the inception of an entity. He noted that the use of the term *implicit* may be enough to require enterprises to consider the power they may hold throughout the life of the entity, depending on certain reconsideration events occurring. He also noted that the examples in the proposed Statement help to prove this point.
7. Mr. L. Smith stated that there is a difference depending on whether there are changes in the structure of the vehicle that result in the enterprise obtaining the

- power in the future versus whether there had been an appropriate assessment of power to begin with and no subsequent changes in the structure of the entity (that is, there are no reconsideration events).
8. Mr. Nickell stated that the Board previously asked the staff to incorporate a paragraph into the standard about skepticism when power and economics are not proportional. He suggested including a disclosure requirement that links directly to that paragraph.
  9. Mr. Roberge stated that the disclosure requirements in paragraph 22A(a) of the proposed amendments require an enterprise to disclose the significant judgments and assumptions made in determining whether the enterprise must consolidate a variable interest entity.
  10. Mr. Linsmeier noted that paragraph 22D(b) of the proposed amendments may help to address Mr. Siegel's concerns. Mr. Siegel stated that it helps ease his concerns that the proposed disclosures reference *implicit arrangements*.

## **Issue 2: Related Party Guidance**

### ***Paragraph 16***

11. Mr. Roberge noted certain constituents were concerned that for purposes of applying the consolidation guidance in paragraph 14 of the proposed amendments to Interpretation 46(R), including shared power, the guidance in paragraph 16(d)(1) indicates that “a party that has an agreement that it cannot sell, transfer, or encumber its interests in the entity without the prior approval of the enterprise” is considered a related party of the enterprise performing the consolidation analysis. Constituents expressed concern that paragraph 16(d)(1) could require many enterprises to consolidate variable interest entities when “power” is, in fact, shared. The primary concern is regarding situations in which mutual transfer restrictions exist in a variable interest entity whereby each investor does not have the ability to transfer its interest without the prior approval of the other party, primarily to preserve the strategic intent of a variable interest entity.

12. **Staff Recommendation:** The staff recommended that the Board amend criterion 16(d)(1) of Interpretation 46(R) to provide an exemption for substantive mutual transfer restrictions as follows (new text is underlined):

A party that has (1) an agreement that it cannot sell, transfer, or encumber its interests in the entity without the prior approval of the enterprise or (2) a close business relationship like the relationship between a professional service provider and one of its significant clients. The right of prior approval creates a de facto agency relationship only if that right could constrain the other party's ability to manage the economic risks or realize the economic rewards from its interests in a variable interest entity through the sale, transfer, or encumbrance of those interests. A de facto agency relationship does not exist if (a) both the enterprise and the party have right of prior approval and such rights are substantive, (b) the rights are based on mutually agreed terms by willing, independent parties, and (c) the rights are not used in an effort to circumvent the provisions of this Interpretation.

Mr. Roberge also emphasized that the existence of a substantive transfer restriction does not obviate the need for each party subject to such a restriction to determine if it is the primary beneficiary of a variable interest entity pursuant to the requirements of paragraph 14 of the proposed amendments.

13. **Board Vote:** The Board unanimously agreed to amend the criterion in paragraph 16(d)(1) of Interpretation 46(R) to provide an exemption for substantive mutual transfer restrictions based on mutually agreed upon terms by willing, independent parties.

14. **Board Comments:** Ms. Seidman asked whether it is more targeted to include this notion in the description of shared power compared with adding it to the assessment of the de facto agency relationship because it seems that the primary application of the exception is in the assessment of shared power.

15. Mr. Roberge stated that the staff considered that suggestion, but he noted that he is not sure that a reporting enterprise would be able to conclude that power is shared because there is also additional guidance requiring consent between parties with shared power. Mr. Nickell stated that the staff was concerned that placing this

concept with shared power would signal that power is shared, which is not what the Board intended.

16. Mr. L. Smith expressed some discomfort with the staff recommendation. Mr. Roberge and Mr. Nickell clarified that the staff recommendation makes the requirement in paragraph 16(d)(1) a mutual requirement, whereas they currently view paragraph 16(d)(1) as a one-way requirement.
17. Mr. Roberge noted that the point of the mutual transfer restriction is to ensure that the entity achieves its business purpose. Mr. Nickell stated that the staff felt that this needed to be stated explicitly because paragraph D43 of Interpretation 46(R) describes a situation in which there is a unilateral right of prior approval where that might be acceptable, but some firms have given guidance saying that it is always a problem.
18. Ms. Seidman also expressed some discomfort with the wording of the staff recommendation in relation to efforts to circumvent the Interpretation, noting that that language should be throughout the document rather than in one specific place. The staff noted that language could potentially be incorporated in the beginning of the standard to apply to the entire document, rather than in select places throughout the document.

***Paragraph 17***

19. Mr. Roberge noted that the staff also received feedback related to the guidance in paragraph 17 of the proposed amendments about removing the quantitative assessment to determine the primary beneficiary from the requirements in paragraph 14 of the proposed amendments.
20. Mr. Roberge also noted that the Board has progressed from a risks-and-rewards approach to a power-plus-risks-and-rewards approach. The staff has received feedback that because the guidance for related parties is also a consolidation test, that enterprises should first look to the guidance proposed within paragraph 14 to identify the party within the related-party group that is the primary beneficiary. If

an enterprise is unable to determine whether it is the primary beneficiary based on the proposed guidance in paragraph 14, then the enterprise would look to the guidance in paragraph 17. Once an enterprise is within the related party guidance, there will always be a primary beneficiary identified.

21. **Staff Recommendation:** The staff recommended that the Board amend paragraph 17 of Interpretation 46(R) to (1) eliminate factors (c) and (e) and (2) require a party within a related party group to first consider whether it is the primary beneficiary through the required consolidation analysis in paragraph 14 of the proposed amendments (except a party within a related party group could not conclude that power is shared). If no party within a related party group meets the criteria in paragraph 14A, the determination of the primary beneficiary shall be based on an analysis of the remaining criteria in paragraph 17 with the objective of determining which party is most closely associated with the VIE. The staff recommended the following drafting changes to paragraph 17 (added text is underlined and deleted text is ~~struck out~~):

If two or more related parties (including the de facto agents described in paragraph 16) hold variable interests in the same variable interest entity, and the aggregate variable interest held by those parties would, if held by a single party, identify that party as the primary beneficiary, then the party, within the related party group, that meets criteria a and b in paragraph 14A is the primary beneficiary. However, a party within a related party group cannot conclude that power is shared pursuant to paragraph 14X. If no single party meets criteria a and b in paragraph 14A, then the primary beneficiary shall be the party within the related party group that is most closely associated with the variable interest entity. ~~is the primary beneficiary~~ The determination of which party within the related party group is most closely associated with the variable interest entity requires judgment and shall be based on an analysis of all relevant facts and circumstances, including:

- a. The existence of a principal-agency relationship between parties within the related party group
- b. The relationship and significance of the activities of the variable interest entity to the various parties within the related party group
- e. ~~A party's exposure to the expected losses of the variable interest entity~~

- d. The design of the variable interest entity
- e. The extent to which a party meets criteria a and b in paragraph 14A.

22. **Board Vote:** The Board unanimously agreed with the staff recommendation subject to the minor drafting changes as suggested by Mr. Golden in paragraph 24 of these minutes.

23. **Board Comments:** Mr. Linsmeier expressed some confusion with the staff recommendation because if an enterprise determines it meets the criteria in paragraph 14A of the proposed amendments and it is the primary beneficiary, then it would not need to go to the related party guidance at all. Mr. Roberge responded that the conclusion in paragraph 14 is that the related-party group, as a whole, is the primary beneficiary. Then the group would move on to the guidance in paragraph 17 to determine which party, within the related-party group, is the primary beneficiary.

24. Mr. Golden suggested that the sentence “If no single party meets criteria a and b in paragraph 14A, then the primary beneficiary shall be the party within the related party group that is most closely associated with the variable interest entity” be added to the beginning of paragraph 17, rather than in the middle as the staff recommended, in order to clarify its meaning.

### **Issue 3: Separate Classification of Elements**

25. Ms. Mathys stated that at the January 2009 Board meeting, the staff recommended that the Board permit, but not require, separate presentation of the elements of consolidated variable interest entities in the primary beneficiary’s financial statements. The Board discussed whether there should be delineation between when certain assets are required to pay off certain liabilities, liabilities are linked to specific assets, or general purpose assets of the consolidating enterprise may be used to fund liabilities of a consolidated variable interest entity. The Board previously requested that the staff to further analyze the issue, including whether separate classification should be permitted or required on the face of the financial statements in certain situations.

26. Ms. Mathys noted that the staff further analyzed this issue, and she presented six alternatives for the Board to consider:

- a. Alternative A – Permit, but do not require, separate classification of all elements of consolidated VIEs on the face of the primary beneficiary’s financial statements.
- b. Alternative B – Require separate classification of all elements of consolidated VIEs on the face of the primary beneficiary’s financial statements.
- c. Alternative C – Require separate classification on the face of the primary beneficiary’s balance sheet for those assets of consolidated VIEs that can only be used to settle obligations of consolidated VIEs.
- d. Alternative C’ – Same as Alternative C and, in addition, require separate classification on the face of the primary beneficiary’s balance sheet for those liabilities of consolidated VIEs for which creditors (or beneficial interest holders) of the consolidated VIE have no recourse to the general credit of the primary beneficiary.

In Alternatives C and C’, separate classification of the remaining elements of the VIE would be permitted, but not required, if it is deemed that such reporting provides more useful information to financial statement users and is not otherwise required by GAAP.

- e. Alternative D – Clarify that the information that is required to be disclosed pursuant to paragraphs 23(b) and 23(c) of the proposed Statement can either be presented in the footnotes or on the face of the financial statements. Also specify that separate classification of the remaining elements of the VIE would be permitted, but not required, if it is deemed that such reporting provides more useful information to financial statement users and is not otherwise required by GAAP.
- f. Alternative E – Require a single line-item display to separately classify both assets and liabilities of consolidated VIEs, with an additional explanation in the notes to the financial statements regarding the composition of the single line item.

27. **Staff Recommendation:** The staff recommended Alternative C’, which is to require separate classification of the elements on the face of the primary beneficiary’s balance sheet for those assets of the consolidated variable interest entities that can only be used to settle the obligations of the consolidated variable interest entities and for those liabilities of consolidated variable interest entities for which creditors (or beneficial interest holders) of the consolidated variable interest entity have no recourse to the general credit of the primary beneficiary. Separate classification of the remaining elements would be permitted, but not required, if it is

- deemed that such reporting provides more useful information to financial statement users and is not otherwise required by GAAP.
28. **Board Vote:** The Board unanimously agreed with the staff recommendation.
  29. **Board Comments:** Mr. L. Smith stated that he agrees with the staff recommendation except for the statement regarding separate classification of the remaining elements being voluntary because that classification is always permitted. Mr. Linsmeier agreed with Mr. L. Smith.
  30. Mr. Herz asked whether there would be further disaggregation of the assets and liabilities of variable interest entities in the footnotes to the financial statements.
  31. Mr. Golden asked whether, under Alternative C', a reporting enterprise would disclose the information rather than be required to separately present the elements on the face of the financial statements, if the assets of the variable interest entity pay off only the liabilities of the variable interest entity but the liabilities of the variable interest entity could also have recourse to the other general assets of the primary beneficiary. Mr. Golden viewed C' as needing both before you would put them on the face of the balance sheet. Mr. Roberge clarified that a reporting enterprise must consider the assets and liabilities separately.
  32. Mr. Herz stated that he would prefer Alternative E because there are cases in which there are non-recourse subsidiaries within the structure of a consolidated entity, and it seems as though a single line-item for both assets and liabilities along with footnote disclosure for additional disaggregation is an easier way to do it. The footnote could discuss which liabilities have recourse to the primary beneficiary's general assets and which do not.
  33. Ms. Seidman stated that in the normal course of business of a securitization, the cash collected must be used to pay the liabilities of the structured vehicle. She stated that this is also a distinguishing feature on the liability side because it is required to occur.
  34. Ms. Seidman also noted the absence of linked presentation as an alternative and she stated that she understands that its absence is consistent with previous Board decisions; however, she pointed out that there are valid reasons for linked presentation, especially under the conditions in the staff's recommendation in

Alternative C'. She asserted that there is an inconsistency between the criteria used to assess the control of the entity and the criteria used to assess control of an asset. It is meaningful to segregate assets that are restricted as to their use and liabilities that are completely limited in terms of the source of repayment possibilities. Therefore, separate presentation as recommended by the staff helps, and there are other similar approaches within GAAP (such as separate accounts of insurance companies, which are presented gross on the balance sheet but regulators rate the risks very differently from the general assets/liabilities of the insurance company). Therefore, if capital requirements are an issue here, then the banking regulators can do the same thing. She believes the criteria in Alternative C' are appropriate and will provide useful information to financial statement users. Discussing other assets and liabilities of the variable interest entity has the potential to cast them as other than available for any use.

35. Mr. Siegel stated that he agrees with the staff recommendation subject to the items discussed at this meeting.
36. Mr. Herz expressed some concern about situations that, over time, develop bright lines on either side of this recommendation, which is why he would have preferred single line-item display with footnote disclosure.

Follow-up Items: None

General Announcements: None