

January 5, 2010

Mr. Russell G. Golden, Technical Director **Financial Accounting Standards Board** 401 Merritt 7 PO Box 5116 Norwalk, CT 06856-5116

Via Email to director@fasb.org

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Re: File Reference No. 1750-100

Dear Mr. Golden:

Grant Thornton LLP appreciates the opportunity to comment on Proposed Accounting Standards Update (ASU), Consolidations (Topic 810)—Amendments to Statement 167 for Certain Investment Funds

We support the proposed deferral for money market funds. However, we have significant concerns about the proposed deferral for other investment companies and the proposed revisions of the guidance on determining whether fees paid to a decision maker or service provided should be considered variable interests. Our concerns and recommendations on these matters are discussed below in our responses to the Questions for Respondents in the proposed ASU.

# Question 1. Do you agree that the Board should defer the effective date of Statement 167 for entities that meet the requirements in the proposed Update?

## Deferral for money market funds

We support the deferral as proposed for a reporting entity's interest in an entity that is required to comply with or that operates in accordance with requirements that are similar to those included in Rule 2a-7 of the Investment Company Act of 1940 for registered money market funds.

# Deferral for other investment companies

We do not support the deferral as proposed for investments companies other than money market funds. We are concerned that the proposed deferral could result in inconsistent consolidation decisions for economically similar arrangements and provide structuring opportunities to avoid consolidation.

The Board proposed this deferral to address users' concerns about the usefulness of investment managers' financial statements if the managers are required to consolidate the investment funds that they manage. However, we believe that similar concerns have been expressed regarding



financial statements of asset managers that already consolidate many entities they manage and would continue to consolidate such entities under FASB Statement 167, *Amendments to FASB Interpretation Na* 46(R), and the proposed ASU.

We believe the proposed deferral raises questions about whether the FASB has articulated the principles of consolidation in Statement 167 in a manner that would result in appropriate, consistent, and comparable consolidation conclusions. For example, consider the following inconsistencies that could arise:

- Power characteristic The manager of a hedge fund or private equity fund that would qualify for
  the proposed deferral might have much greater discretion over the management of that
  fund's assets, and therefore greater power to direct activities that to impact the economic
  performance of that fund, than the manager of a collateralized debt obligation (CDO) has
  over the assets and economic performance of a CDO that would not qualify for the deferral.
- Economic characteristic: An asset manager's right to receive benefits from a variable interest entity (VIE) that are potentially significant to the VIE, without an obligation to absorb significant losses of the VIE is a characteristic that could lead to the asset manager's consolidation of a VIE that does not qualify for the proposed deferral, but not to the asset manager's consolidation of a VIE that qualifies for the proposed deferral.
- Fiduciary arrangements: Statement 167 guidance on determining the primary beneficiary of a VIE, together with the guidance on determining whether fees paid to a decision maker or service provider, are expected to appropriately identify purely fiduciary arrangements that should not result in consolidation by the fiduciary. The proposed deferral indicates that guidance is not sufficient to prevent consolidation of fiduciary arrangements with entities that would qualify for the deferral. It is not clear why such guidance could be expected to consistently and appropriately identify fiduciary relationships with entities that would not qualify for the proposed deferral.

We believe that the proposed deferral, like any exception to an accounting principle, would encourage efforts to design structures to qualify for the deferral and off-balance sheet accounting because of the inconsistencies noted above and the difficulty in determining which entities qualify for the deferral.

### International convergence

The Board indicated that the proposed deferral would address concerns that the Statement 167 consolidation guidance for entities that qualify for the deferral might change under the joint IASB/FASB consolidations project. However, the possibility that a converged standard could differ significantly from Statement 167 was known when Statement 167 was adopted. Furthermore, there is no assurance that the entities that qualify for the proposed deferral would be the only entities affected by a final converged consolidation standard.



#### Recommendation

We recommend that the Board not adopt the deferral as proposed for entities other than money market funds. However, we agree that the asset manager of a mutual fund generally should not consolidate that fund. We suggest that the Board consider whether a deferral for mutual funds could be articulated in a manner similar to that in the proposed deferral for money market funds. If not, then the Board should consider whether Statement 167 should be more broadly deferred than it would be under the proposed deferral.

Our responses to question 2 identify issues that we believe the Board should address if it decides to adopt the deferral as proposed.

Question 2. Do you believe that the amendments to paragraph 810-10-65-2 in this proposed Update clearly identify the population of entities that would qualify for the deferral?

As indicated in our response to question 1, we do not support the deferral as proposed for entities other than money market funds. However, if the Board decides to adopt the deferral as proposed, then we recommend that the Board

- Move guidance critical to the clarity and consistent application of the deferral from the proposed ASU's Basis for Conclusions to the authoritative Codification text
- Revise the proposed effective date and transition requirements for a change in facts and circumstances that results in an entity ceasing to qualify for the deferral

# Guidance in the proposed ASU's Basis for Conclusions

The proposed ASU's Basis for Conclusions contains nonauthoritative guidance that appears to be critical to the understanding and consistent application of the proposed deferral in accordance with the Board's intentions. Such guidance should be included in the authoritative Codification text, not relegated to the nonauthoritative Basis for Conclusions section. Although we appreciate the Board's efforts to keep the authoritative text of the Codification principle-based, the Board's use of the nonauthoritative Basis for Conclusions to create de facto rules or interpretations that are essential to the appropriate application of a principle raises questions about the sufficiency of the guidance in the authoritative text.

Definitions of asset-backed financings and investment companies Paragraph BC9 in the proposed ASU's Basis for Conclusion states the following:

The Board has concluded that an entity with multiple levels of subordinated investors, for example, a collateralized debt obligation or collateralized loan obligation for which the primary purpose of the capital structure of the entity is to provide credit enhancement to senior interest holders, would not qualify for the deferral. The Board considers entities with this type of capital structure to be asset-backed financing entities rather than investment companies.



The Board appears to be using the proposed nonauthoritative guidance in paragraph BC9 to create new guidance on identifying an investment company and on defining an asset-backed financing. The Board provided this guidance for the purpose of clarifying the intended scope of the proposed deferral. However, we believe that it is not appropriate for the Board to expect constituents to apply guidance in the Basis for Conclusions as though it were authoritative. Nor do we believe that the Board should effectively create a new definition of an "investment company" for the deferral in FASB Accounting Standards Codification<sup>TM</sup> (ASC) Topic 810 that differs from the definition/description in ASC Topic 946, *Financial Services—Investment Companies*.

#### Recommendation

If the Board expects constituents to apply the guidance in paragraph BC9 of the proposed ASU, then the Board should provide authoritative guidance using one of the following alternatives:

- Amend ASC 946-10-15-2 to indicate that an entity with multiple levels of subordinated investors is not an investment company. However, we do not recommend this alternative unless the Board comprehensively considers and deliberates the effects of changing the scope of the guidance in ASC Topic 946.
- Explain why the deferral could apply to an entity with a single level of investors, but not to an entity with multiple levels of investors, and include the following sentence in the proposed guidance in ASC 810-10-65-2(aa)(1):
  - An entity with multiple levels of subordinated investors, for example, a collateralized debt obligation or collateralized loan obligation for which the primary purpose of the capital structure of the entity is to provide credit enhancement to senior interest holders, would not qualify for the deferral.
- Consider whether defining an asset-backed financing as in paragraph BC9 of the proposed ASU could impact the application of other guidance, such as ASC Topic 860, *Transfers and Servicing* which uses the term *asset-backed financing* in its application and disclosure requirements.

Variable interest entities in Statement 167 examples
Paragraph BC10 in the proposed ASU's Basis for Conclusions states the following:

In addition, the examples included in the implementation guidance in Statement 167 are not modified as a result of the amendments in this proposed Update. Accordingly, the Board concluded that an entity that has the characteristics consistent with those of a variable interest entity in the implementation guidance of Statement 167 should not be subject to the deferral as provided in this proposed Update.

A deferral of an accounting standard usually does not change the provisions of that standard, but instead defers the application of those provisions for a specified population. Therefore, we



think it is inappropriate to assume that constituents would understand that the proposed deferral of Statement 167 should not apply to any variable interest entities described in Statement 167's implementation guidance examples solely because the proposed Update does not modify those examples.

#### Recommendation

If the Board expects constituents to apply the guidance in paragraph BC10 of the proposed ASU, then the Board should include the following sentence in the proposed guidance in ASC 810-10-65-2(aa)(1):

An entity that has characteristics consistent with those of a variable interest entity in [insert links to the relevant codified examples from the implementation guidance of Statement 167] should not be subject to the deferral as provided in this subparagraph.

Obligation to fund losses of the entity that could potentially be significant. An investment company other than a money market fund would not qualify for the proposed deferral if the reporting entity has an obligation to fund losses of the entity that could potentially be significant to the entity. Proposed guidance on this condition in ASC 810-10-65-2(aa)(1)(ii) states, "This condition should be evaluated considering any implicit or explicit guarantees provided by the reporting entity and its related parties, if any." Although that sentence requires "consideration" of guarantees, it does not explicitly state how such guarantees should be considered or that any such guarantees should always disqualify an investment company from the proposed deferral. However, paragraph BC6 in the Basis for Conclusions of the proposed ASU states:

[T]he Board believes that in situations in which a reporting entity has explicitly (through contract or a legal requirement) or implicitly guaranteed the debt of an investment fund, this guarantee is considered to be a potential funding of losses of the entity and, accordingly, would disqualify the entity from the deferral provided by this proposed Update.

Thus, the Board appears to be trying to establish in the nonauthoritative basis for conclusions a presumption for how certain guarantees should be considered in accordance with the proposed authoritative text.

### Recommendation

Any guidance intended to create a rule or presumption for considering how certain guarantees affect an entity's qualification for the deferral should be provided in the authoritative text rather than in the nonauthoritative Basis for Conclusions.

Effective date and transition for an entity that loses its deferral We do not support the proposed effective date and transition requirements in proposed subparagraph ASC 810-10-65-2(aa) for an entity that initially qualifies for the proposed deferral, but subsequently ceases to qualify because of a change in facts and circumstances.



#### Effective date

Proposed subparagraph ASC 810-10-65-2(aa) states, "Public and nonpublic entities shall provide the disclosures required by the pending content in paragraphs 810-10-50-1 through 50-19 for all variable interests in variable interest entities that qualify for the deferral in this subparagraph. An entity that initially meets the deferral requirements of this subsection may subsequently cease to qualify as a result of a change in facts and circumstances. In such a situation, the pending content that links to this paragraph shall be effective for the reporting entity as set forth in item (a)." The effective date for pending content linked to item (a) in ASC 810-10-65-2 would be as of the beginning of the first annual reporting period, and interim periods within that annual period, that begins after November 15, 2009, which is the original effective date of Statement 167.

Therefore, under the proposed guidance, the deferral might cease to apply to a VIE, for example, because a law enacted two years after Statement 167's original effective date imposes an obligation on the reporting entity to fund potentially significant losses of that VIE. Although the conditions of the deferral were met until the new law created a new obligation, the reporting entity would retroactively lose the deferral for that VIE.

#### Transition

Proposed subparagraph ASC 810-20-65-29(aa) also states, "If the reporting entity is required to consolidate an entity because that entity no longer qualifies for the deferral, the reporting entity shall initially measure the assets, liabilities, and noncontrolling interests of the VIE in accordance with paragraphs 810-10-30-1 through 30-6."

Those paragraphs, ASC 810-10-30-1 through 30-6, provide the ongoing guidance for the initial consolidation of a VIE, rather than the special transition guidance for the initial consolidation or deconsolidation of a VIE upon adoption of Statement 167. Therefore, none of the special transition guidance for the initial adoption of Statement 167 would apply to the initial consolidation of a VIE that ceases to qualify for the deferral after Statement 167's original effective date. For example, the fair value option in ASC 810-10-65-2(d), otherwise available for a VIE initially consolidated as a result of adopting Statement 167, could not be elected for a VIE that must be consolidated as of January 1, 2010 solely because the VIE ceased to quality for the deferral in 2012.

#### Recommendations

We recommend that if a change in facts and circumstances results in a VIE ceasing to qualify for the deferral, a reporting entity should be required to initially apply the previously deferred provisions of Statement 167 to that VIE as of the date of the change, not as of the date when Statement 167 would have originally applied absent the deferral. Recognizing the effect of a change as of the date of the change would be consistent with the recognition of other reconsiderations of whether an entity is a VIE or whether a reporting entity is the primary beneficiary of a VIE. Therefore, we suggest that the proposed guidance in ASC 810-10-65-2(aa) be revised as follows (suggested additions are underlined, deletions are struck-through):



aa. Except for the disclosures required by the pending content in paragraphs 810-10-50-1 through 50-19, the pending content that links to this paragraph shall not be applied to either of the following: ...

The deferral in this subparagraph does not apply to disclosures required by pending content in paragraphs 810-10-50-1 through 50-19. Therefore, reporting entities Public and nonpublic entities shall provide the disclosures required by the pending content in paragraphs 810-10-50-1 through 50-19 for all variable interests in variable interest entities that qualify for the deferral in this subparagraph. An entity that initially meets the deferral requirements of this subsection may subsequently cease to qualify as a result of a change in facts and circumstances. In such a situation, the pending content deferred by this subparagraph that links to this paragraph shall be effective for the reporting entity's interest in that entity as of the date the entity ceases to qualify for the deferral, set forth in item (a).

We also recommend that the FASB consider whether any of the special Statement 167 transition provisions in ASC 810-10-65-2(b) through (i), rather than the guidance in ASC 810-10-30-1 through 30-6, should apply when a VIE subsequently ceases to qualify for the deferral. Even if the Board decides to retain the proposed effective date and transition requirements for the subsequent loss of a deferral, we believe the Board should address the availability of a fair value option election in those circumstances.

Question 3. Do you believe that the Board's proposed change to include language to clarify that related-party arrangements should be considered for all of the conditions in paragraph B22 of Statement 167 is operational and achieves the Board's objectives?

Effective date for revisions to paragraph B22 guidance We are concerned about the effective date proposed for substantive revisions to the pending guidance in ASC 810-10-55-37 (formerly paragraph B22 of FASB Interpretation 46(R), as amended by Statement 167.) Issued in June 2009, Statement 167's effective date provided a reporting entity at least five months to implement the new standard. Both Statement 167 and the proposed ASU would be effective as of January 1, 2010 for SEC registrants with a calendar year-end. Such registrants will be expected (a) to provide robust disclosures about the impact of adopting Statement 167 and the proposed ASU in their financial reports for the year ended December 31, 2009 and (b) to issue March 31, 2010 financial statements in accordance with the Statement and proposed ASU.

For many reporting entities, implementation of Statement 167 requires extensive information gathering and analysis. Depending on the conclusions reached in such analyses, adopting Statement 167 may require significant modifications of a reporting entity's financial reports, and financial reporting processes, procedures and controls. In order to meet their obligations for timely financial statement issuance, many reporting entities will have completed their analysis of Statement 167's impact on existing arrangements before the FASB finalizes any guidance in the proposed ASU in 2010. The issuance of a final ASU in January 2010 would allow many reporting entities only a few weeks, rather than a few months, to read, understand, and implement the new guidance. The population of reporting entities affected by the guidance on



determining whether a decision maker's or service provider's fee arrangement is a variable interest is extensive and is not limited to asset managers or investment companies. Therefore, we believe that the Board should provide adequate time for implementing changes to the guidance in paragraph B22 that could significantly affect the analysis required or alter consolidation or disclosure conclusions previously reached by constituents in a reasonable, good faith effort to implement Statement 167 on a timely basis.

#### Recommendation

If the proposed or other substantive revisions to the guidance in paragraph B22 are issued in final form in early 2010, we recommend that the revised guidance become effective for interim and annual reporting periods beginning on or after June 15, 2010.

# Clarification of consideration of related party interests

The proposed guidance in ASC 810-10-55-37A does not indicate how a related party's interests should be considered in the application of ASC 810-10-55-37. For example, must all fees paid under any arrangement between a VIE and a related party group be aggregated for analysis of each condition? If so, could the result of such analysis be that one or more, but not all, of the related party group's fee arrangements is a variable interest, or must the same conclusion apply to all of the related party group's fee arrangements?

#### Recommendation

If the Board decides to adopt the proposed guidance in ASC 810-10-55-37A, we suggest that the Board consider whether additional guidance is needed to clarify how related party interests should be considered in the assessment of the conditions in the pending content in ASC 810-10-55-37. (See responses to question 4 for additional discussion of related party considerations for assessment of the proposed content in ASC 810-10-55-37(c).)

Question 4. Do you believe that the Board's proposed changes to condition(c) in paragraph B22 of Statement 167 are operational and achieve the Board's original objective in Statement 167 that a qualitative test should not be the sole determinant of whether a fee arrangement is a variable interest?

We do not support the proposed amendments to the guidance for condition (c) in the pending content of ASC 810-10-55-37 (formerly paragraph B22 of Interpretation 46(R), as amended by Statement 167), for reasons discussed below.

# Interests held by related parties

We do not support eliminating the phrase "and its related parties, if any" from condition (c) in the pending content of ASC 810-10-55-37. The meaning and context of the eliminated phrase is not identical to that of the new general requirement in proposed ASC 810-10-55-37A to consider any interest in the entity held by a decision maker's or service provider's related parties for the purpose of evaluating all of the conditions in ASC 810-10-55-37. As a result, the proposed ASU would reduce the clarity of condition (c) and could, in fact, fundamentally change the level at which interests might be aggregated for the assessment of significance.



Condition (c), before amendment by the proposed ASU, explicitly requires all variable interests in an entity held by a decision maker or service provider (other than the decision maker's or service provider's fee arrangement) to be aggregated with interests in that entity held by the decision maker's or service provider's related parties. Condition (c) is not met if those interests in aggregate would absorb a more than insignificant amount of the entity's expected variability. Although the revised guidance under the proposed ASU would require consideration of interests in the VIE held by related parties, it would not explicitly require all such interests to be aggregated with those of the decision maker or service provider for the significance assessment in condition (c). Without the phrase "and its related parties" in condition (c), a decision maker might consider its related parties' interests in the VIE by assessing whether each related party's aggregate interests would absorb a significant amount of the VIE's variability. Therefore, under the proposed ASU, the decision maker might conclude that condition (c) is met if no individual entity within the related party group would absorb significant expected variability of the VIE, without considering whether the aggregate interests of the related party group as a whole would absorb significant expected variability of the VIE.

### Recommendations

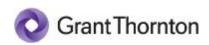
We recommend that the phrase "and its related parties, if any" be retained in the pending content of ASC 810-10-55-37(c) (formerly condition (c) in paragraph B22 of Interpretation 46(R), as amended by Statement 167). The elimination of that phrase would neither clarify nor improve the existing guidance, even with the addition of the proposed guidance on consideration of related party interests in ASC 810-10-55-37A.

Expected losses, expected residual return, and expected variability The proposed ASU would add the following sentence to the pending content in ASC 810-10-55-37(c):

For the purposes of this subparagraph, the quantitative approach described in the definitions of the terms expected losses, expected residual returns, and expected variability, is not required and should not be the sole determinant as to whether a reporting entity has such obligations or rights.

However, neither Statement 167 (as codified) nor the proposed ASU would change the following:

- Definitions of expected losses, expected residual returns, and expected variability
- Definition of variable interests as "investments or other interests that will absorb portions of a variable interest entity's (VIE's) expected losses or receive portions of the entity's expected residual returns"
- Guidance that permits, and sometimes requires, a quantitative assessment of expected losses to determine whether an entity is a VIE because it lacks sufficient equity investment at risk



In addition, neither Statement 167 nor the proposed ASU provides any guidance or illustrative examples on how to qualitatively determine whether or not variable interests would absorb more than an insignificant amount of the VIE's expected losses or expected residual returns.

Therefore, under a reasonable, good faith interpretation of the authoritative text of Statement 167, a reporting entity could have based its conclusions of significance for paragraph B22(c), as amended by Statement 167, on quantitative estimates of expected losses, expected residual returns, and expected variability. As indicated in our response to question 3, many reporting entities will have completed the analysis required for timely implementation of Statement 167 before the guidance in the proposed ASU can be finalized in 2010.

We believe that the proposed requirement for a qualitative assessment and the prohibition of reliance on a quantitative assessment for condition (c) would represent a substantive change to, rather than clarification of, the provisions of Statement 167. Therefore, the effective date for such changes should provide adequate time for implementation.

We do not believe the proposed qualitative assessment of the significance of expected losses and expected residual returns would be operational without additional guidance. Furthermore, we note that when Interpretation 46(R) established the requirement for a qualitative analysis of the sufficiency of an entity's equity investment at risk, paragraph 9 of the Interpretation provided examples of such qualitative assessments, but acknowledged that a reasonable estimate of expected losses might be necessary and sufficient when a qualitative assessment is not determinative. Therefore, we question the Board's presumption that it would always be possible to determine qualitatively whether or not variable interests would absorb a more than insignificant amount of an entity's expected losses or receive more than an insignificant amount of an entity's expected residual returns, especially when a quantitative analysis is necessary to determine that an entity is a VIE.

The Board has acknowledged that the Statement 167 guidance intended to identify fiduciary relationships, including guidance in paragraph B22, may not be directionally consistent with the guidance issued as a result of the joint FASB/IASB project to develop a converged standard on consolidation. This may be true even if the Board adopts the revisions to the guidance in paragraph B22, as proposed. Therefore, we do not support adopting at this time the proposed revisions that could effectively negate efforts to issue financial statements on a timely basis using a reasonable, good faith interpretation of the published authoritative guidance.

# Recommendation

The pending content in ASC 810-10-55-37(c) should not be further amended at this time to require a qualitative assessment and to prohibit placing sole reliance on a quantitative assessment based on the definitions of expected losses, expected residual returns, and expected variability.

If the Board decides to adopt the proposed requirement for a qualitative assessment of whether or not variable interests would absorb a more than insignificant amount of a VIE's expected losses or expected residual returns, then we recommend that the Board



- Provide additional guidance for, or examples of, such a qualitative assessment and not prohibit reliance on a quantitative assessment if a qualitative assessment is not determinative. Alternatively, change the wording of the condition in the pending content in ASC 810-10-55-37(c) to be consistent with the wording of the financial characteristic of a primary beneficiary in the pending content in ASC 810-10-25-38A(b) (formerly paragraph 14A(b) of Interpretation 46(R), as amended by Statement 167) if a reporting entity is expected to apply the qualitative assessment guidance for ASC 810-10-25-38A(b) to assessments of significance under the pending text in ASC 810-10-55-37(c).
- Provide sufficient time for implementation of any changes to the existing guidance, which is
  effective as of January 1, 2010 for many entities. Changes to the nature of assessments
  required to determine if the condition in the pending content in ASC 810-10-55-37(c) is met
  would be substantive, could be widely applicable, and could require significant time to
  understand and implement.

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We would be pleased to discuss our comments with you. If you have any questions, please contact Mark Scoles, Partner, Accounting Principles Consulting Group, at 312.602.8780, or Ann McIntosh, Senior Manager, Accounting Principles Consulting Group, at 612.677.5257.

Sincerely,

/s/ Grant Thornton LLP