

**Proposed FSP—Treatment of fees paid to decision makers and guarantors in determining expected losses and expected residual returns of a variable interest entity under FASB Interpretation No. 46, *Consolidation of Variable Interest Entities*.**

**(Comment Deadline: May 26, 2003)**

Q—How do fees paid by a variable interest entity to a decision maker or provider of a guarantee of substantially all of the entity's assets or liabilities affect the determination of the primary beneficiary of a variable interest entity?

A—The expected losses of a variable interest entity have two components: (a) the expected unfavorable variability in the variable interest entity's net income or loss and (b) the expected unfavorable variability in the fair value of entity's assets, if that variability is not included in the variability of net income or loss. Fees paid to decision makers and guarantors are deducted in determining net income or loss and require no further adjustment. If a variable interest or combination of interests of a single enterprise (with consideration of interests held by its related parties and de facto agents) will absorb a majority of the expected losses if they occur, that enterprise is the primary beneficiary, and it is not necessary to compute expected residual returns.

If the analysis of expected losses does not identify a primary beneficiary, expected residual returns must be analyzed. The expected residual returns of the entity include four components if they are present in the entity:

- a. The expected favorable variability in the entity's net income or loss
- b. The expected favorable variability in the fair values of the entity's assets (if that variability is not included in variability of net income or loss)
- c. The total fees paid to the decision maker for the entity (if there is a decision maker)
- d. The total fees paid to providers of guarantees (including writers of put options and other instruments with similar results) of all or substantially all of the entity's assets or liabilities or both.