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December 1, 2003

Mr. Lawrence W. Smith  
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Financial Accounting Standards Board  
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Letter of Comment No: 82  
File Reference: 1082-300  
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Re: File Reference 1082-300

Exposure Draft for Proposed Interpretation – Consolidation of Variable Interest Entities, a modification of FASB Interpretation No. 46

Dear Mr. Smith:

We appreciate the opportunity to provide comments on the Exposure Draft for the Proposed Interpretation – *Consolidation of Variable Interest Entities, a modification of FASB Interpretation No. 46* (the "Exposure Draft"). We further appreciate FASB's willingness to address certain technical corrections and implementation issues that have arisen with FASB Interpretation No. 46, *Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51* (FIN 46). However, we have concerns that many of the proposals in the Exposure Draft are unclear and FASB's effort to address FIN 46 implementation issues is being undertaken in a piecemeal manner. The Exposure Draft notes that additional guidance on certain issues may or may not be issued in the future and there are concurrently separate FASB Staff Positions (FSPs) attempting to address key issues. Furthermore, a comment period of 30 days is inadequate to fully assess and comment on the proposed changes. We strongly support the alternative view of certain Board members that this Exposure Draft and the implementation of FIN 46 be deferred until all the issues have been adequately addressed. We further suggest that guidance be re-issued in one comprehensive document, so that constituents have the opportunity to evaluate the guidance as a whole. Our specific comments on the Exposure Draft are as follows.

### Scope Exception for Certain Mutual Funds

It is unclear what types of "mutual funds" are supposed to meet the scope exclusion and why. In the US, the term mutual fund is generally used to describe an open-end management investment company as defined in the Investment Company Act of 1940. The *AICPA Audit and Accounting Guide – Audits of Investment Companies* states that "investment companies are organized as corporations (in the case of mutual funds, under the laws of certain states that authorize the issuance of common shares redeemable on demand of individual shareholders) and common law trusts (sometimes called business trusts)....", among others. The only conceptual basis provided in the Exposure Draft as to why mutual funds in trust form should be scoped out from FIN 46 is that they are, by their design, customary practice, and law, not for the

benefit of the trustee, therefore the Board did not expect trustees to be deemed to be the primary beneficiaries of those trusts. We agree with this point, but based on this rationale it is unclear why mutual funds in other forms would not also be scoped out from FIN 46 and we would suggest that the scope exception should apply to all mutual funds regardless of their form.

### **Reevaluation of VIE Determination and Primary Beneficiary**

In FIN 46, FASB required reevaluation of the VIE determination and primary beneficiary status only upon certain reconsideration events rather than every reporting period. FASB agreed with respondents that the information necessary to reevaluate might not be available or would be burdensome to acquire. The proposed changes in the Exposure Draft that would require reevaluation as a result of changes in the design of the entity or ownership interests will effectively require that enterprises make an effort to acquire the necessary information that was originally agreed to be difficult or burdensome to acquire. Yet the Exposure Draft does not address how the issue of obtaining the necessary information would no longer be a problem or how this problem could be mitigated. We suggest that this proposed change in the Exposure Draft be deleted, or at minimum guidance be provided to mitigate the impossibility or difficulty of acquiring this information. If the Board chooses to issue further guidance, we would suggest the Board avoid the use of ambiguous language, such as the language used in the prior FIN 46 exposure draft that proposed that an enterprise was not required to conduct an "exhaustive search" for information<sup>1</sup>.

### **Expected Losses and Expected Residual Returns**

It is unclear how to interpret the proposed guidance that expected losses and expected residual returns include the expected variability in the entity's "long-term return to variable interests." The Exposure Draft does not provide an explanation as to why short-term returns should be ignored when assessing which party has a majority of the expected losses and expected residual returns. We believe that all returns to variable interest holders should be considered in accordance with the techniques an enterprise determines appropriate when evaluating expected losses and expected residual returns. We suggest revising "long-term return to variable interests" to "all returns to variable interests."

We support the clarification that qualitative factors should be emphasized over quantitative calculations when determining whether the equity investment at risk is sufficient. We also support FASB not specifying a single technique or otherwise limiting an enterprise's ability to choose techniques it believes are appropriate when evaluating whether it will absorb a majority of the entity's expected losses, expected residual returns, or both. However, the Exposure Draft alludes to the fact that the Board may in the future specify a single technique or otherwise limit an enterprise's ability to choose a technique for evaluating an entity's expected losses and expected residual returns. To avoid further confusion, we suggest that the Exposure Draft be delayed until the Board is certain whether or not it wishes to issue such guidance in the near future. If guidance is issued, it should be part of one comprehensive document that is re-released for comment.

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<sup>1</sup> We support the proposed scope exclusion for certain entities created before February 1, 2003, but have similar concerns regarding the use of the ambiguous language "exhaustive effort" in paragraph 4.g of the Exposure Draft.

Complicating this issue further is the fact that there are separate FSPs attempting to address the treatment of certain decision maker fees. We originally thought FSP FIN 46-7, *Exclusion of Certain Decision Maker Fees from Paragraph 8(c) of FASB Interpretation No. 46, Consolidation of Variable Interest Entities* (FSP FIN 46-7) was the final version of proposed FSP FIN 46-c<sup>2</sup> and FSP FIN 46-d<sup>3</sup>. However, we note that FSP FIN 46-d is still outstanding on the FASB website. Many of the criteria in FSP FIN 46-7 are substantially different than those included in either FSP FIN 46-c or FSP FIN 46-d and constituents will never have an adequate opportunity to comment on this guidance if it were included as part of a final interpretation that was not re-released for comment. We further find the opening question to FSP FIN 46-7 difficult to understand as it states that paragraph 8(c) of FIN 46 requires fees to be paid to a decision maker to be included in the calculation of an entity's expected residual returns. We agree that this was the interpretation of how decision maker fees should be treated. However, our interpretation for this treatment of decision maker fees was pursuant to paragraph B9 of FIN 46, which is now deleted in the Exposure Draft. We believe that this is another example of the confusion being caused by the piecemeal manner in which FIN 46 guidance is being promulgated, which supports the alternative view that this Exposure Draft and the implementation of FIN 46 should be deferred until all the issues have been adequately addressed in one comprehensive document.

## Appendix B

We agree that in some respects it is difficult to interpret the descriptions of variable interests provided in Appendix B. However until the Board provides further guidance, paragraphs B1 through B10 are the only detailed explanations that exist about variable interests. These explanations are crucial to the understanding of this standard, so we suggest that the Exposure Draft be delayed until the Board completes the revised guidance on variable interests and that the guidance should be included as part of one comprehensive document.

## Transition

Many of the proposals in the Exposure Draft are unclear, which adds complexity to an already complex standard. The Exposure Draft alludes to future guidance that may or may not be issued, which may require preparers to again change their good faith application of FIN 46 in the near future. There are separate FSPs on FIN 46 concurrently being issued or still outstanding, making it difficult to fully consider the proposed changes in this Exposure Draft. Considering these issues, a 30-day comment period is inadequate to assess the proposed changes. We also find it difficult to understand how the FASB will adequately consider respondents' comments and address the issues for an effective date for the first reporting period ending after December 15, 2003. We strongly support the alternative view of certain Board members that this Exposure Draft and the implementation of FIN 46 be deferred until all the issues have been adequately addressed. We further suggest that this guidance be re-issued in one comprehensive document, so that constituents have the opportunity to evaluate the guidance as a whole.

<sup>2</sup> Proposed FSP FIN 46-c, *Impact of Kick-Out Rights Associated with the Decision Maker on the Computation of Expected Residual Returns under Paragraph 8(c) of FASB Interpretation No. 46, Consolidation of Variable Interest Entities* (FSP FIN 46-c).

<sup>3</sup> Proposed FSP FIN 46-d, *Treatment of Fees Paid to Decision Makers and Guarantors as Described in Paragraph 8 in Determining Expected Losses and Expected Residual Returns of a Variable Interest Entity under FASB Interpretation No. 46, Consolidation of Variable Interest Entities* (FSP FIN 46-d).

December 1, 2003

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If you have any questions regarding this letter, please call me (212-250-2660) or James Curry (212-250-1973) or send an electronic message to: [accounting.policygroup@db.com](mailto:accounting.policygroup@db.com).

Very truly yours,

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