American International Group, Inc. 70 Pine Street New York, N.Y. 10270

June 1, 1999

Mr. Timothy Lucas
Director of Research and Technical Activities
Financial Accounting Standards Board
401 Merritt 7
P. O. Box 5116
Norwalk, CT 06856-5116

Letter of Comment No: /02
File Reference: 1082-194R
Date Received: 6/8/99

RE: Exposure Draft (Revised) - Consolidated Financial Statements: Purpose and Policy File Reference No. 194-B

Dear Mr. Lucas:

We appreciate the opportunity to respond to the captioned Exposure Draft (ED).

The general rule governing consolidation of subsidiaries contained in FASB Statement No. 94 (FAS 94) relates to a controlling financial interest based on a direct or indirect ownership of a majority voting interest of over fifty percent of the outstanding voting shares of another company. This rule has worked reasonably well in practice.

FAS 94 eliminated the "nonhomongeneity exception" and thus provided more comprehensive and more meaningful financial statements. However, FAS 94 did not address the control of entities by means other than majority ownership of voting securities. The proposed concept that the financial statements should include the assets, liabilities, operations, and cash flows of all entities controlled by the issuer is sound. Correspondingly, there is a need for a broader definition of control as well as implementation guidance.

Changing the standard for consolidation from a majority voting interest to a standard based on control, as defined in the ED, is in essence moving from a simple fact based test to a test based on the use of judgement in evaluation of the facts and circumstances. The amount of judgement required will vary depending upon the complexities of particular facts and circumstances.

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Our specific comments with respect to the ED are as follows:

- There should only be one rebuttable presumption of control. This should be limited to circumstances where an entity has a majority voting interest in the election of another entity's governing body or a right to appoint a majority of the members of its governing body, as described in paragraph 18(a). The three additional situations cited as presumptions of control, described in paragraphs 18(b), 18(c) and 21, are more appropriately considered indications of control. Where minority voting interests are held, demonstrable evidence of control should exist before an entity should be required to be consolidated. The situations cited in paragraphs 18(b), 18(c) and 21 rely on presumptions and expectations of future events or actions. Under such circumstances, it is far better to wait until the ability to control has been demonstrated rather than to consolidate an entity based on assumptions of expected actions only to be required in subsequent periods to adjust the accounting, when it was determined that the assumptions made as to control were not correct. The foregoing position is in substantial agreement with Alternative View, paragraphs 248 to 256.
- In situations where the equity ownership is very small, unless the facts indicating control are clear, consolidation would result in an inappropriate gross up of assets and liabilities with little effect on results of operations. The consolidation would be even less meaningful, if debt was secured by the property with no recourse to the owners. Under such circumstances, summarized financial data would seem more appropriate.
- Due to the many complexities surrounding SPE's, the ED should be expanded to include greater discussion of related issues and additional illustrations provided.
- As mentioned previously, the implementation of the standards contained in the ED require a great deal more judgement than existing standards. The good faith judgements made by management, as long as they are considered reasonable under the facts and circumstances, should be considered acceptable until demonstrated otherwise.

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We appreciate this opportunity to express our views which are submitted in a constructive manner, and hope that they prove helpful to the Board in its consideration of this standard.

Very truly yours,

Howard I. Smith

Executive Vice President,

Chief Financial Officer and Comptroller

HIS/cb