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California  
Society  
Certified  
Public  
Accountants

February 15, 1996

Financial Accounting Standards Board  
Director of Research and Technical Activities  
File Reference 154-D  
401 Merritt 7  
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Dear Committee Members:

The Accounting Principles and Auditing Standards Committee of the California Society of Certified Public Accountants ("AP & AS Committee") has discussed the exposure draft of the proposed Statement of Financial Accounting Standards, *Consolidated Financial Statements: Policy and Procedures*, dated October 15, 1995 and has several comments about the proposed standard.

The AP & AS Committee is a senior technical committee of our state society. The committee is comprised of 50 members, of which 14 percent are from national CPA firms, 54 percent are from local or regional firms, 24 percent are sole practitioners in public practice, 4 percent are in industry, and 4 percent are in academia.

Our committee overwhelmingly agreed with the approach that consolidation be based on the concept of control. We do not believe, however, that the definition of control is operational.

We have two major problems with the operational use of control for purposes of determining which subsidiaries to consolidate. First, we believe that this is a major change to financial presentations. We believe that the current model of financial statements representing financial matters of the voting owners of the financial statements is well understood and certainly historically established. Changing the landscape of financial statements to recognize financial matters under common control is too significant to be readily understood by financial statement readers—particularly in cases involving real estate limited partnerships and not-for-profit entities. We are very concerned that this major change would be prohibitively costly and cumbersome for smaller, more closely-held organizations.

Financial Accounting Standards Board  
February 15, 1996  
Page 2

Second, we are very concerned that the definition of control may allow the same company to be consolidated by different parents. This may not be such an unusual circumstance as each parent would make their determination independently. The world of control-basis financial statements may spawn new battlegrounds for competing companies to claim domination. Any definition of control must have some level of subjectivity to it. Financial statement preparers and auditors, mindful of their duty to faithfully follow FASB rules, may consolidate the same subsidiary into two different parents. Likely troublesome scenarios include a major shareholder with a less than a 50 percent stake but possessing a kicker of some kind (convertible debt, for example) vs. a 51 percent shareholder or major positions (20 percent or more) held by competitors each with some additional claim of control (number of directors, contracts or other financial arrangements).

For these reasons we do not agree that the exposure draft should be issued as a Financial Accounting Standard. We believe that a more workable approach would be to amend FAS 94 for the most troublesome areas. We believe that the FAS 94 approach works very well for situations involving entities with a clearly delineated voting/equity stake. The troublesome areas seem to be in the areas of not-for-profit entities and certain partnerships (or other form of entity) where voting stake is different than the ownership (or profit sharing) stake. For the reasons discussed above, we believe that consolidating these entities is too major a change to the financial landscape to be operational. We propose that the amendment to FAS 94 include supplemental footnote disclosure of, among other things, the assets and liabilities, nature of business and relationship of the entities not consolidated because they involve entities without a clearly delineated voting/equity stake.

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The committee appreciates the opportunity to respond and hopes that these points assist you in your deliberations. The committee will be happy to clarify any of the points raised.

Sincerely,



Jessie C. Powell, Chair  
Accounting Principles and Auditing Standards Committee  
California Society of Certified Public Accountants

cc: Jim Kurtz, Executive Director  
Gale Case, Society President