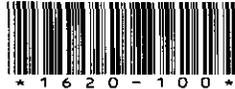




October 30, 2008

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



LETTER OF COMMENT NO. 19

**File Reference No. 1620-100**

Dear Mr. Golden:

Thank you for the opportunity to comment on the Proposed Statement of Financial Accounting Standards, *Amendments to FASB Interpretation No. 46(R)* (the "Exposure Draft"). This letter is being submitted jointly on behalf of the American Securitization Forum (ASF)<sup>1</sup> and the Securities Industry and Financial Markets Association (SIFMA)<sup>2</sup>. We fully support FASB's efforts to improve financial reporting by enterprises involved with variable interest entities and to provide more relevant and reliable information to users of financial statements. However, we are concerned that the changes proposed in the Exposure Draft do not entirely meet those objectives.

Timing and Convergence

We strongly believe that FASB's best course of action would be to reconsider the proposed changes and consider other alternatives, with an emphasis on international convergence. We continue to believe that FASB's understandable haste to respond to the current market crises is inhibiting the ability of FASB and affected constituents to adequately consider and debate the

<sup>1</sup> The ASF is a broadly-based professional forum of participants in the U.S. securitization market. Among other roles, the ASF members act as issuers, underwriters, dealers, investors, servicers and professional advisors working on securitization transactions. This comment letter was developed principally in consultation with the ASF's Accounting Committee, with input from other ASF members, subforums and committees. More information about the ASF, the Accounting Committee and their respective members and activities may be found at the ASF's internet website, located at [www.americansecuritization.com](http://www.americansecuritization.com).

<sup>2</sup> SIFMA brings together the shared interests of more than 650 securities firms, banks and asset managers. SIFMA's mission is to promote policies and practices that work to expand and perfect markets, foster the development of new products and services and create efficiencies for member firms, while preserving and enhancing the public's trust and confidence in the markets and the industry. SIFMA works to represent its members' interests locally and globally. It has offices in New York, Washington D.C., and London and its associated firm, the Asia Securities Industry and Financial Markets Association, is based in Hong Kong.

merits of the very significant changes that FASB is proposing. While, in retrospect, many users of financial statements feel that existing policies led to insufficient disclosure of reporting enterprises' contingent exposures to variable interest entities (VIEs), we are concerned that the revised standard would frequently require consolidation where the reporting enterprise does not have the level of control that users of financial statements typically associate with consolidated assets.

FASB has responded in some measure to timing concerns by extending the effective date of the proposed changes to January 1, 2010. However, we continue to believe that FASB should use the additional time to extend its deliberations on the optimal consolidation policy for VIEs. The incremental disclosures already being provided by many enterprises, as supplemented by the requirements of the proposed new disclosure FSP (on which we have commented separately), answer the interim need for greater transparency.

FASB should also take advantage of the additional time to strive for international convergence on these important matters. The international scope and importance of the structured finance markets has been demonstrated beyond doubt by the ripple effects from the recent problems in US subprime residential mortgage lending. With both FASB and the International Accounting Standards Board (IASB) currently engaged in projects on consolidation, working on standards that generate similar results and on relatively similar time frames, FASB and IASB should go the extra mile and truly converge by producing a single standard. With international convergence becoming a reality, FASB should strive to avoid putting preparers and users of US GAAP financial statements through a profound set of interim changes.

We have done our best, in light of the brief comment period, to provide specific, concrete comments on the changes proposed in the Exposure Draft. However, given the magnitude of the changes being proposed, we note that the condensed comment period was challenging for us and other constituents to consider fully not only the changes proposed in the Exposure Draft, but also the related changes to Statement 140 and the interim disclosure FSP. Accordingly, we underscore again that our primary recommendations are the ones set out above under "Timing and Convergence," and the balance of our recommendations below would ideally not be our last input in this process. In these circumstances, our specific comments on the Exposure Draft are as follows.

As an overall matter, we are concerned that the proposed changes would result in consolidation of VIEs by enterprises that do not have control over the VIEs commensurate with the control exercised by the parent of an entity consolidated under ARB 51 and related guidance. For instance, the primary beneficiary of a VIE rarely has the unilateral ability to prepay the VIE's liabilities in order to refinance, sell or otherwise deploy the related assets. As a result, financial statements prepared in accordance with the proposed changes would combine assets where the reporting enterprise has materially different levels of control and would combine liabilities without regard to whether they are general liabilities payable from truly controlled assets or instead are payable primarily from cash flows of assets that are not truly owned or controlled by the reporting enterprise.

In many cases, this will result in the consolidation of assets that are not available to the creditors of the reporting enterprise and not subject to control in a manner that would normally be

expected by equity investors. A prime example is managers of collateralized debt obligations (CDOs). These enterprises frequently combine “power to direct matters that most significantly impact the activities of” the CDO issuer (a VIE), including “activities that impact the entity’s economic performance”, with a small minority stake in the subordinated tranches. While holding far less than a majority of the economic residual, a manager’s subordinated investment might entitle the manager to benefits that might be considered to “potentially be significant to the variable interest entity”, as required by paragraph 14A(b). Indeed, Example 2 in the Exposure Draft examines a situation of this type and requires consolidation. As a result, if the Exposure Draft is adopted without significant modifications, it is likely that we will see these entities issuing financial statements that are less representationally faithful in nature. Users of financial statements will be forced to estimate which assets are truly controlled and which liabilities are payable from those assets by resorting to footnote disclosures, other available information and *more or less informed speculation*.

### Linked Presentation Proposal

As more fully described below, we believe that the changes proposed in the Exposure Draft would result in a significant increase in the number of VIEs that must be consolidated. In many cases, *the consolidation decision will be highly judgmental, and reasonable investors may conclude that the assets, liabilities and other displayed attributes of some or all of these entities should be viewed differently from the assets, liabilities and other attributes of traditional consolidated operating subsidiaries.* As a result, we believe investors will be better served by a transparent presentation on the face of the balance sheet (and other financial statements) of the effect of such consolidation, which would clearly indicate which assets are segregated to support which liabilities. Accordingly, we believe that a serious exploration of linked presentation is not only feasible but well worth undertaking at this time.

Ideally, the scope and details of the linked presentation would be worked out in the context of extended deliberations on all the changes proposed in the Exposure Draft, with a goal of converging with the IASB at the time that the changes go into effect. In case FASB continues on the announced schedule, we make a proposal on scope and provide some initial thoughts on the mechanics of a linked presentation in Attachment 1. We would be happy to engage with FASB and its staff to further operationalize the concept.

### Definition of Control

The following comments are offered in response to the Exposure Draft as written. We support an approach that looks for both power and an economic interest in a qualitative assessment. We believe, however, that both factors are defined too broadly in the Exposure Draft:

- As to power, the examples in the Appendix lead one to believe that the power customarily exercised by a servicer of consumer loans may be sufficient to trigger this factor under the proposed language. We recognize that FASB has struggled greatly to decide how much discretion is too much in the servicing context. Given the complexity of that judgment, it does not seem appropriate to treat all servicing as tantamount to control. We believe that an ideal control standard would not equate routine, rules-driven servicing with control.

- At a minimum, we request additional guidance on analyzing situations where control is shared. For instance, consider the following two examples:
  - Example A. Assume a single transferor transfers loans to a special purpose entity (SPE) and takes back the economic residual but services only 40% of the loans. Servicing for the remaining 60% of the loans is divided equally among three other servicers, each of which originated its serviced loans and previously sold them to the transferor on a servicing-retained basis and in a manner that satisfied the requirements of paragraph 9 of Statement 140. In our view, the transferor in this scenario does not satisfy the power requirement, since the powers to direct matters that significantly impact the activities of the SPE are shared.
  - Example B. Assume that three unaffiliated entities provide services to a single municipal auction rate trust: one sources portfolio investments for the trust, the second is responsible for credit analysis and approval and the third markets and remarkets the beneficial interests in the trust. We submit that it may be reasonable to conclude that no one of these three activities “most significantly” impacts the trust’s activities, including its economic performance, and consequently no one party should be deemed to be the primary beneficiary of the trust.
- Also relevant to the topic of shared power is FASB’s proposed treatment of substantive kick-out rights. We believe that FASB underestimates the practical significance of substantive kick-out rights, even where collective action is necessary for their exercise. FASB has recognized the significance of these rights when held by a single entity and, in other contexts, when held in a manner that requires collective action for their exercise. We see no reason to create this inconsistency in GAAP and ignore these important and substantive rights. The qualitative judgment required by the proposed new standards provides ample opportunity for auditors to challenge non-substantive arrangements, without creating this per se rule that ignores these arrangements even when entered into in good faith. We request that FASB revise paragraph 14A(a) to require consideration of all substantive kick-out rights, and rely on the qualitative nature of the determination to avoid abuse.
- As to economic interest, we believe that requiring only potential, as opposed to actual, significance, is problematic in that “potential” is too diffuse and subjective a term. For example, how far into the future, and what sorts of scenarios, and at what probability levels, would enterprises need to consider? We request that FASB revise paragraph 14A(b) to change the standard from *potentially* significant to *presently* significant. The fact that enterprises would be required to continuously re-evaluate the status of a VIE would presumably capture any future changes in economic benefits and risks, without requiring enterprises to make a probability assessment of their occurrence at the outset. If FASB is concerned about potential exposure to losses that might result from reputational risks, we believe that factor can, and should, be considered in determining the present significance of a variable interest.

We recognize that these are hard lines to draw, and in the limited time allowed for comments, we have not reached consensus on the optimal definitions. Even with the improvements suggested

above, we believe some level of over-consolidation would be inevitable. Consequently, we have focused our energies on refining a linked presentation proposal, which can mitigate the difficult all-or-nothing nature of the consolidation decision for at least those VIEs where the consolidation decision is most judgmental.

#### Eliminating the Back-Up Quantitative Test

Given FASB's strong preference for the qualitative approach under proposed paragraphs 14A and 14B, we struggle to find practical examples where it will be appropriate to move to the fallback quantitative analysis under proposed paragraph 14C. We believe that including the quantitative fallback is likely to lead to confusion and overuse of the fallback, since preparers and their auditors may cling to the perceived objectivity of a quantitative test. Therefore, we request that FASB eliminate paragraph 14C and leave the qualitative test as the only one.

#### Transition

Among the VIEs that are likely to be consolidated under the proposed new standards are credit card master trusts that currently are scoped out of Interpretation 46(R) as qualifying special purpose entities. The consolidation of these entities will create some difficult transition issues, especially if FASB does not adopt a linked presentation or an entity of this type falls outside of the scope of any linked presentation that is adopted.

Under the proposed transition rules, the primary beneficiary would measure and recognize at fair value the credit card receivables held by the VIE at the time of consolidation. However, subsequently arising credit card receivables will be booked at par (in the absence of some other fair value election or requirement). This split in valuation methods for similar assets is likely to create anomalies in reporting and diminish the transparency of the issuer's financial statements.

We have not been able to reach consensus on the best solution to this issue in the time allowed for comments on the Exposure Draft. We believe that the impact would be mitigated by our linked presentation proposal. We would also be happy to work with FASB's staff in further delineating this issue and assessing possible solutions.

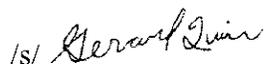
\* \* \* \* \*

Thank you again for the opportunity to comment on the Exposure Draft. Please contact George Miller, Executive Director of the American Securitization Forum at 212.313.1116, or Gerard Quinn, Managing Director & Associate General Counsel of the Securities Industry and Financial Markets Association at 212.313.1207 with any questions or comments.

Sincerely,



George P. Miller, Executive Director  
American Securitization Forum



Gerard J. Quinn, Managing Director  
and Associate General Counsel  
Securities Industry and Financial Markets Association

## Overview of the Linked Presentation

### Scope

We propose that enterprises be required to use a linked presentation for consolidated, bankruptcy remote VIEs, the activities of which are limited to incurring asset-backed liabilities, owning or holding the pool of assets that support or service the liabilities and other activities reasonably incidental to the foregoing. For this purpose, “asset-backed liabilities” should be defined as liabilities that are expected to be paid primarily from (1) cash flows of an identified pool of restricted financial assets, (2) proceeds of additional liabilities which are expected to be paid primarily from the same sources and (3) any payments received under any related interest rate or currency derivatives. Any recourse to other assets of the consolidated group would be subject to meaningful qualitative and/or quantitative limits (to be determined). Financial assets may be added to the pool or disposed of, and the VIE may incur additional liabilities, in each case to the extent permitted by the terms of the asset-backed liabilities and related documents. Cash flows include collections from obligors, recoveries and proceeds from disposition of related collateral or the financial assets themselves. VIEs subject to the linked presentation may hold non-financial assets that are reasonably incidental to the holding of their financial assets, including servicing rights and nonfinancial assets obtained through collecting financial assets.

Our proposed scope is meant to implement a principle that, when specified financial assets are dedicated to paying specific liabilities, and those liabilities are expected to be paid primarily from the proceeds of those assets, the best presentation is to link the specified assets and liabilities. It is also meant to apply to many securitization SPEs that are not currently consolidated by an enterprise, because under current guidance either they are qualifying SPEs or the enterprise is not the primary beneficiary. We recognize that with additional time it might be possible to refine the scope. Under the current time constraints, however, we believe that applying a linked presentation to many newly consolidated securitization SPEs is appropriate.

### Fair Value

Enterprises would be required to carry at fair value the assets and liabilities of consolidated VIEs that were subject to the linked presentation.