

December 10, 2012

Susan M. Cospers
Technical Director
Financial Accounting Standards Board
401 Merritt 7
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Norwalk, CT 06856-5116

Via email: director@fasb.org

Re: Proposed Accounting Standards Update, *Consolidation (Topic 810): Accounting for the Difference between the Fair Value of the Assets and the Fair Value of the Liabilities of a Consolidated Collateralized Financing Entity* (File Reference No. EITF-12G)

Dear Ms. Cospers:

This letter represents the comments of certain members (see list on page 5) of the Asset Management Industry Accounting Policy Group (“AMIAPG”), comprising a forum of companies primarily engaged in the asset management business. The AMIAPG companies represented by this letter include both publicly-traded and privately-held asset managers who collectively manage more than 5,100 investment funds, both domestically and internationally, including registered investment companies, hedge funds, private equity funds, exchange-traded funds and collective investment trusts, in addition to separate accounts and other sponsored investment products. The three companies represented by this letter collectively have subsidiaries registered as investment advisors, broker/dealers, trust banks and insurance companies, and oversee approximately \$5 trillion of assets under management.

We appreciate the opportunity to provide comments to the Financial Accounting Standards Board (the “FASB” or the “Board”) on the Proposed Accounting Standards Update (“ASU”), *Consolidation (Topic 810): Accounting for the Difference between the Fair Value of the Assets and the Fair Value of the Liabilities of a Consolidated Collateralized Financing Entity* (“the Proposal” or the “Proposed ASU”). We commend the work of the Board to address the diversity in practice in measuring the fair value of the assets and liabilities of collateralized financing entities consolidated in accordance with the consolidation accounting guidance for variable interest entities within FASB Accounting Standards Codification (“ASC”), *Consolidation (Topic 810)*.

We believe that the use of the net risk exposure as fair value measurement for the assets and liabilities of the collateralized financing entities may be preferable if the following primary areas of concern regarding the Proposed ASU are clarified:

- I. Scope and Definition of Collateralized Financing Entities:** The definition of a collateralized financing entity should include entities with nominal non-participating, non-voting equity shares or temporary ownership of non-financial assets.
- II. Practical Application for Determining the Net Risk Exposure of Collateralized Financing Entities:** The allocation of the fair value to the respective assets or liabilities of a collateralized financing entity requires additional clarification and transitional guidance to ensure the results intended by the Board are consistently achieved.

III. Application of Fair Value Measurements Guidance and Disclosures: It is unclear how the fair value of the assets or liabilities, which are based on the more determinable fair value of either the assets or liabilities, would be classified in the fair value hierarchy in accordance with ASC Topic No. 820, *Fair Value Measurements* (“ASC 820”).

I. Scope and Definition of Collateralized Financing Entity

The Proposed ASU contains an amendment to the Master Glossary which defines a collateralized financing entity (“CFE”) as “A variable interest entity that holds debt instruments, issues beneficial interests in those financial assets, and has no equity. All of the beneficial interests are financial liabilities that only have recourse to the related financial assets of the collateralized financing entity.” We note certain CFEs issue nominal equity instruments that are non-participating and non-voting equity shares, which are typically issued to meet local incorporation requirements. ASC Topic No. 505, “*Equity*” (“ASC 505”) defines equity as the residual interest in the assets of an entity that remains after deducting its liabilities. It appears non-participating and non-voting nominal equity shares would not meet the definition of equity as defined in ASC 505. Accordingly, we request the Board to clarify its intent to include within the scope of the Proposal, CFEs that issue such nominal equity instruments.

Additionally, the proposed definition of a CFE contemplates that the CFE only holds financial assets. In the event the CFE temporarily holds non-financial assets (for example, collateral received in exchange for defaulted debt securities), the CFE could potentially be precluded from applying the guidance in the Proposed ASU. We suggest that the Board add specific purpose and design considerations to the definition of a CFE so that an entity that would have otherwise met the definition of a CFE and temporarily holds nonfinancial assets may also apply the proposed guidance.

The scope of the Proposed ASU is limited to CFEs for which the fair value option has been elected. We suggest that the FASB address the accounting model for a consolidated CFE when a fair value option is not made. Under an amortized cost model the carry values of the CFE assets and liabilities will diverge over time with the difference included in the reporting entities retained earnings and the changes in the assets and liabilities included in the net income attributable to the reporting entity. This is true whether or not the reporting entity owns a beneficial interest. This accounting model does not reflect the results that a reporting entity would ultimately expect to realize and should be corrected at the same time the fair value model is corrected.

II. Practical Application for Determining the Net Risk Exposure of CFEs

We agree with the FASB's proposal that the fair value of the assets and liabilities presented should be based on the more determinable fair value of either the financial assets or the financial liabilities when the reporting entity owns none of the CFE's beneficial interests. ASC 820-10-35-18F provides that a reporting entity may need to allocate the portfolio-level adjustments to the individual assets or liabilities that make up the group of financial assets and financial liabilities managed on the basis of the reporting entity's net risk exposure. A reporting entity shall perform such allocations on a reasonable and consistent basis using a methodology appropriate in the circumstances.

We propose the Board require a relative fair value allocation approach in allocating the portfolio-level adjustments to individual assets or financial liabilities in order to avoid diversity in practice. Existing accounting guidance within ASC 805 “*Business Combinations*” and ASC 350 “*Intangibles – Goodwill and Other*” either requires or permits the use of a relative fair value allocation approach in the following situations:

- a) Acquisition of assets - allocation of the cost to individual assets (or individual assets and liabilities) that make up the group based on their relative fair values and does not give rise to goodwill.

- b) Allocation of acquired assets and assumed liabilities to a reporting unit - acquired assets and assumed liabilities employed in or related to the operations of multiple reporting units shall be assigned to each reporting unit. The methodology used to determine the amount of those assets or liabilities assigned to a reporting unit shall be reasonable and supportable and shall be applied in a consistent manner. One acceptable approach is based on the relative fair values of the different reporting units.
- c) Allocation of goodwill to a reporting unit - when an entity reorganizes its reporting structure or when a portion of a reporting unit is to be disposed of, goodwill shall be reassigned to the reporting units affected using a relative fair value allocation approach.
- d) Allocation of goodwill impairment loss between parent and non-controlling interest - if a goodwill impairment test results in an impairment loss, such loss shall be allocated between the parent and the non-controlling interest on a “rational basis”. Acceptable methods may include the following:
 - i. Allocate impairment losses on the basis of the relative fair values, as of the acquisition date, of the parent and the non-controlling interest.
 - ii. Allocate impairment losses on the basis of the relative fair values, as of the impairment testing date, of the parent and the non-controlling interest.

In the event a reporting entity owns some of the beneficial interests of a CFE, it is unclear how a market participant would fair value a reporting entity’s net risk exposure. Paragraph BC6 states that “the fair value of the beneficial interests held by the reporting entity should be determined based on the perspective of market participants, consistent with the objective of measuring the net amount that the reporting entity would expect to realize if it has (or believes it can readily obtain) the means to terminate the CFE, that is, to sell the CFE’s assets, settle the CFE’s obligations, and realize the net amount.” This guidance implies that the reporting entity would use a liquidation basis method of estimating the value of its net risk exposure. Currently, an investment manager may use an income approach to measure its beneficial interest in a CFE using assumptions that are consistent with ASC 820-10-35-3A regarding an orderly transaction between market participants to sell or transfer the interest.

The liquidation approach and the income approach may result in different valuations, as under current guidance, beneficial interests are priced assuming the CFE is a going concern (i.e., beneficial interests are not priced to the earliest call date as of the balance sheet date). The valuation of the outstanding beneficial interests issued (i.e., the liabilities of the consolidated CFE) determined utilizing the liquidation approach will, in most cases, not be the same as the fair value of the reporting entity’s retained beneficial interests recorded by the standalone entity and therefore, the consolidation entries will result in an incorrect elimination of the reporting entity’s beneficial interests. As an additional point, we note in paragraph BC9 of the proposed ASU, *Presentation of Financial Statements (Topic 205), The Liquidation Basis of Accounting*, an acknowledgement that the liquidation basis of accounting may require significant estimation and could result in measurement that differs from fair value. Further, in this situation where a reporting entity owns some of the beneficial interests in the CFE, once such a valuation is determined for the reporting entity’s net risk exposure, it is unclear how this valuation would be allocated to the individual financial assets and financial liabilities of the CFE.

III. Application of Fair Value Measurements Guidance and Disclosures

The exception permitted to ASC 820-10-35-18 does not provide clear guidance on how the fair value hierarchy should be applied under ASC 820-10-35. First, the financial assets and liabilities on a standalone basis may be classified differently among the hierarchy levels (e.g., either a level 1 asset or a level 2 or 3 liability) than they would be on a net basis. If the fair value is based on how a market participant would price the net risk exposure, one could conclude that the classification among hierarchy levels should be determined in a manner consistent with this net exposure.

For example, as discussed in Section II above, in cases where the reporting entity does not own a portion of the beneficial interests of the CFE, the more determinable fair value of either the financial assets or financial

liabilities is used to allocate the portfolio-level adjustments to the individual assets or liabilities that make up the group of financial assets and financial liabilities managed on a net basis. There is a presumption in this scenario that the fair value hierarchy disclosures would only be relevant for that more determinable fair value group – either the financial assets or the financial liabilities.

Alternatively, when the reporting entity owns some of the beneficial interests of a CFE and values the net exposure using a liquidation basis method, it is unclear how this valuation would be allocated to the individual financial assets and financial liabilities of the CFE and therefore if the fair value hierarchy disclosures would be required at all.

Second, it is unclear as to how the changes in hierarchy levels during the reporting period due to the allocation of the portfolio-level adjustments to either the financial assets or financial liabilities be attributed (e.g., as transfers in and/or out of level 3 due to changes in the observability of significant inputs).

We suggest the Board provide additional clarity in this regard to avoid divergence in practice in both determination of the hierarchy levels and related disclosures.

IV. Other

Transition and Early Adoption

We agree with the inclusion of both the modified retrospective and full retrospective approaches for transition and are supportive of early adoption. We do not anticipate significant costs or time to be incurred as a result of the adoption and implementation of the Proposed ASU.

Application to Non-Public Reporting Entities

We believe that the amendments should apply to both public and non-public reporting entities to avoid further diversity in practice among reporting entities as well as differences between a parent's consolidated and subsidiary's standalone financial results.

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We appreciate the opportunity to provide comments on the Proposed ASU. Should you have any questions, please feel free to contact any of the representatives below.

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