MINUTES

Financial Accounting Standards Board

To:	Board Members		
From:	Statement 140 and Interpretation 46(R) Teams (Mathys, ext. 446)		
Subject:	Minutes of the November 6, 2008, Roundtable Meeting: Statement 140 and Interpretation 46(R)	**Date:**	February 9, 2009
cc:	FASB: Golden, Bielstein, Lott, Donoghue, Lusniak, Mayer, Yust, Sperry, Barker, Roberge, Hood, Chookaszian, Posta, Schonefeld, Gabriele, Sutay, Glotzer, Allen, Klimek, C. Smith, Mechanick, Nickell, Reager, Mathys, Cropsey, Proestakes, Wilkins, Stoklosa, FASB Intranet; IASB: Leisenring, Kusi-Yeboah, Teixeira		

The Roundtable minutes are provided for the information and convenience of constituents who want to follow the Board's deliberations. All of the conclusions reported are tentative and may be changed at future Board meetings. Decisions become final only after a formal written ballot to issue a final Statement, Interpretation, or FASB Staff Position.

Topic: Statement 140 and Interpretation 46(R) Amendments Roundtable—Afternoon Session

Basis for Discussion: Amendments to Statement 140 and Interpretation 46(R)

Length of Discussion: 1:00 p.m. to 3:30 p.m.

Attendance:

Board members present:	Herz, Linsmeier, Seidman, L. Smith, and Siegel
Staff in charge of topic:	Donoghue, Roberge, Mayer, and Nickel
Other staff at Board table:	FASB: Golden and C. Smith IASB: Teixeira
Participants:	Howard Shapiro, Fox-Pit Kelton; Jane Knopf, Northeast Utilities; Tim Kviz, Freddie Mac; Huy Tran, MBIA; Steve Buller, BlackRock; Mark Scoles, Grant Thornton; Mark LaMonte, Moody's; Steve Merriett, Federal Reserve; Hal Schroeder, Carlson Capital; Jim Kroeker, SEC; Tom Barbieri, PwC; Judy O'Dell, PCFR; James Campbell, Wellington Management; Seth Grosshandler, LSTA; Patrick Finnegan, CFA Institute; Matt Waldron, CFA Institute; Tony Sondhi, CFA Institute; Eric Janson, AICPA-TIC ; Richard Johns, Capital One

Objective of Meeting:

1. The objective of this meeting was to solicit feedback from constituents regarding the proposed FASB Statements, *Accounting for Transfers of Financial Assets*, and *Amendments to FASB Interpretation No. 49(R)*, and FASB Staff Position (FSP) FAS 140-4 and FIN 46(R)-8, *Disclosures by Public Entities (Enterprises) about Transfers of Financial Assets and Interests in Variable Interest Entities*.

AMENDMENTS TO STATEMENT 140

2. Mr. Golden opened the meeting and stated that the objective of the proposed Statement on accounting for transfers of financial assets is to improve the relevance and representational faithfulness of reporting transfers of financial assets. The significant improvements accomplished by the proposals include (a) the elimination of the qualifying special-purpose entity concept, (b) a definition of *participating interest*, and (c) improvements to how to consider legal isolation.

Issue 1: Whether the Proposals Meet the Objective of the Project

1. Mr. Schroeder stated that the objective of the project is appropriate and that the proposals are consistent with that objective and will improve financial reporting. He also stated that this is the ideal time to make changes, and he would encourage the Board to make changes sooner rather than later.

2. Mr. Johns stated that he does not disagree with the objective of the project; however, the activities of plain-vanilla securitizations, which were clearly envisioned under the FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, have not changed since the inception of the standard. Therefore, he supports a financial components approach and the qualified special-purpose entity concept as a way to define the requisite control that should be allowed by a servicer. While he acknowledged that the definition of a qualified special-purpose entity has been stretched recently, he does not believe it has been by the credit card or auto

industries. He is supportive of slight changes to the standard, but requests that the Board leave as much of Statement 140 in tact as possible because it is a good standard.

3. Mr. Waldron stated that the proposed changes to amend Statement 140 make substantial improvements. However, he would prefer more of a "risk-and-rewards" perspective rather than centering derecognition around legal isolation.

4. Mr. Kviz expressed concern over a number of issues with the proposal. On the whole, he does not see the proposals as an improvement in financial reporting because they will result in more transactions qualifying for sale accounting than currently do, and more of those transactions will become consolidated than do today. He is particularly concerned that the different control thresholds in the derecognition and consolidation standards will result in consolidation of transfers that were accounted for as sales. He feels that this could mislead investors.

5. Mr. Barbieri stated that, generally, the proposed changes represent an improvement. However, he had concerns similar to those of Mr. Kviz; the proposals add complexity because there is no clear principle around the concept of "control." This causes conflicting results with regard to securitization vehicles because if an entity meets all the derecognition criteria for its transferred assets, but then also "effectively controls" that entity from a FASB Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities*, perspective, it will have to consolidate the entity when all the entity does is handle and collect cash from those assets.

Issue 2: Participating Interest

6. Mr. Grosshandler stated that, in general, the definition of participating interest meets the needs of Loan Syndications and Trading Association. However, he questioned whether the notion of a participating interest is necessary, and he noted that a number of other comment letters raised a similar issue. From a legal isolation perspective, there is no reason why one would only need to have

proportionate interests. For example, the sale of a senior interest or a sale of only the interest or principle may still meet legal isolation. If the Board decided to go that route, it would dispel some of the detailed issues that Loan Syndications and Trading Association has over the definition of participating.

7. Mr. Johns requested additional guidance for revolving trusts. He stated that, in a revolving trust, which meets the definition of a variable interest entity, an enterprise transfers a whole group of assets to the trust and then the enterprise takes back an additional beneficial interest in that trust in the form of seller's interest. He requested clarification regarding (a) whether that would classify as a wholly-owned transfer in the first transfer and (b) whether the taking back of the beneficial interest would classify as a participating interest.

8. Ms. Donoghue stated that the enterprise could get sale accounting (that is, qualify as a participating interest) for the first transfer to the revolving trust because it relinquishes control as long as the enterprise is not deemed to be the primary beneficiary under the consolidation guidance.

9. Mr. Kviz stated that with the proposed Statement on accounting for transfers of financial assets, and the interplay between Statement 140 and the proposed Statement on amendments to Interpretation 46(R), Ginny Mae would have to analyze certain structures to determine whether they are sales of participating interests, even though it is selling an undivided interest that is a straight pass-through of the cash flows of the loan, except for the servicing fee (which is permitted in the definition of a participating interest) and the guarantee fee that is paid to Ginny Mae (which is not permitted). Now, the Ginny Mae securitization, which was previously accounted for as a sale, must be accounted for as a financing. The economic substance of the two arrangements is identical.

10. Ms. Seidman asked whether that issue could be remedied by the Board broadening what could be included as a "fee for service" while not tainting the definition of *participating interest*.

11. Mr. Kviz stated that Ms. Seidman's suggestion could potentially solve the problem. Another way to solve the participating interest aspect of the issue would be to allow other things, such as transaction fees to be considered in the definition of *participating interest*.

12. Mr. Grosshandler stated that his understanding of the exposure draft on the amendments to Statement 140 is that up-front fees should not affect the enterprise's permanent cash flow. If, in fact, they do, then that would be an issue for Loan Syndications and Trading Association because there are a lot of fees that are paid up front in the context of corporate loans that are not passed through to participants.

13. Mr. Barbieri disagreed that participating interest, as defined, appropriately represents the economics of transactions. He questioned the exclusion of hybrid instruments in which there is a derivative instrument that does not seem to be clearly and closely related. He stated that there could be many hybrids for which one could carve out the cash flows, and there would not be any additional decision-making that could not be split evenly. He also struggled with how to deal with certain decisions that would be made, such as a put-right or a contingent put-right, from a practice perspective. Finally, he expressed concern with servicing and the concept of subordination. It is unclear whether an enterprise could have a servicing fee that might in theory be subordinate to certain cash flows.

Issue 3: Proposed Amendments to Paragraph 9(a) – Legal Isolation

14. Mr. Golden asked how valuing an implicit arrangement should be handled for disclosure purposes and how it would impact the concept of legal isolation in the proposed amendments to paragraph 9(a).

15. Mr. Grosshandler stated that the legal analysis would consider implicit arrangements. However, if an enterprise does not have an obligation to stand ready to buy back securities in order to protect its reputation, it would not be

viewed as recourse from a true-sale perspective. If an enterprise discloses that it is likely to support the trust, the implicit obligation would still not affect the ultimate true-sale conclusion because it is not a written obligation and the company can always step back and decide not to support the trust.

16. Mr. Schroeder expressed concern over having a very strict legal definition that may not consider side agreements. From an analytical standpoint, users believe a company will make the business decision to protect its reputation and will, therefore, take back some assets, which begs the question of whether the enterprise really ever sold them. He stated that showing these “half-sold” assets on the balance sheet through linked presentation would be ideal.

17. Mr. Finnegan stated that there has been too much emphasis on the legal perspective, and if the goal is to present the underlying economic picture and not just the legal picture, then there must be some analysis of both the legal perspective and the economic relationship with the entity.

18. Mr. Herz stated that the changes to paragraph 9(c) of Statement 140 expands the standard to consider whether an enterprise essentially retains control, rather than only looking at it from the legal perspective, to consider whether an enterprise essentially retains control.

Issue 4: Elimination of QSPE

19. Mr. Scoles stated that he agrees that the qualified special purpose entity structure has been broken for a long time, and it should be eliminated.

20. Mr. Johns stated that plain-vanilla securitizations should still be allowed an exemption from Interpretation 46R because there is no real control over the entities. The consequence of eliminating the qualified special purpose entity concept is that trillions of dollars of securitizations will be consolidated even though the control is really more “influence” than “power.” This causes

consolidation as opposed to recognizing that the true risk-and-reward profile has not changed at all.

21. Mr. Waldron stated that financial statements with more on the balance sheet are more transparent. He is not concerned that elimination of the qualified special purpose entity concept would cause over-consolidation.

22. Mr. Schroeder stated that he supports linked presentation on the balance sheet. He also stated that it is possible to have a linked balance sheet, income statement, and statement of cash flows, and there are no major problems in disaggregating the balance sheet or the income statement.

23. Mr. Johns stated that he, too, is supportive of separate presentation on the balance sheet. However, he is concerned that putting all assets on the balance sheet is equally as misleading as putting no assets on the balance sheet because it would show more assets than are truly controlled by the enterprise. Linked presentation with "net" assets would allow the enterprise to show assets that it actually has claims over.

24. Mr. Finnegan stated that he would prefer a linked presentation on a gross basis. He expressed concern with the concept of having some control or influence vs. "true control" as Mr. Johns described it. Mr. Finnegan believes that if there is **any** control, the assets should not be derecognized. If derecognition of some assets and liabilities with some continuing involvement is allowed, he stated that he supports a linked presentation that shows continuing involvement on the face of the balance sheet on a gross basis with disclosure in the footnotes in order to give the user the full appreciation of the level of activity that is occurring over time.

25. Mr. LaMonte agreed with Mr. Finnegan that assets should be displayed in a linked presentation. He stated that bringing the assets back on the balance sheet and effectively disclosing the risks associated with the assets will allow investors

to more accurately understand how much capital an enterprise needs to support its business.

26. Mr. Kviz stated that government sponsored enterprises only own the credit risk associated with the loans they guarantee, and they account for that credit risk clearly in the financial statements. However, if the government sponsored enterprise were to include loans and third party debt on its balance sheet, the interest income and expense (which is not owned by the government sponsored enterprise) will outweigh the credit component, and therefore will not reflect the true substance of the business.

27. Mr. Merriett stated that reconsidering the capital rules in response to the accounting changes is also a challenge because to apply a fixed capital charge against all of the assets that may come on to the balance sheet does not seem to make a lot of sense for some of these transactions. Transparency is very important in determining what risk is involved in loans that have been securitized because these loans are different from those held in a portfolio, so there is no reason to assign the same risk rating to both.

28. Mr. Schroeder stated that it is important to be able to see the information trends on the balance sheet over longer time periods, so he would prefer restatements for any change in the accounting rules in order to not lose that ability to assess trends. Mr. LaMonte and Mr. Sondhi agreed.

Issue 5: Proposed Change to Paragraph 9(c)3

29. Mr. Kviz stated that the proposed changes to paragraph 9(c)3 are operational for government sponsored enterprises.

30. Mr. Barbieri agreed that the changes are operational and represent an improvement on the current standard.

31. Mr. Johns inquired about the order in which the consolidation/derecognition standards should be applied. Ms. Donoghue replied that to do the isolation

analysis, an enterprise must conduct the consolidation analysis; therefore, in most cases it is more efficient (but not required) to do the Interpretation 46R analysis first.

32. Mr. Kviz stated that the discussion of the Guaranteed Mortgage Securitization structure in the basis of conclusions seems to imply that a guaranteed mortgage securitization is a swap-and-hold and fails sale accounting, but if the structure is applied against paragraph 9 of the proposed Statement, it will meet the requirement for sale accounting. He inquired whether it was the Board's intent that a swap-and-hold transaction would not meet sale accounting.

33. Ms. Donoghue responded that the intent of that exception was to put Guaranteed Mortgage Securitization structures on a level playing field with other similar transactions in the marketplace.

AMENDMENTS TO INTERPRETATION 46(R)

34. Mr. Golden began discussion about FIN 46(R) and opened a dialogue about the objective and whether the proposed FIN 46(R) model meets that objective. He said that he wanted to talk about the qualitative assessment and ongoing reassessment.

Issue 1: Objective

35. Mr. Waldron said that the qualitative approach is an improvement. Mr. Buller stated that he supports the qualitative approach, but there are issues with the mechanics of the qualitative approach. He said that as an investment advisor, there are a number of issues raised in the qualitative approach. He stated that one of the issues is that it is hard to argue that an advisor is not involved in activities that effect the VIE even though the role is that of a service provider on behalf of third party investors.

36. Mr. Buller stated that the IASB is deliberating whether a service provider should be carved out of the consolidation guidance. He said that when referring to the

right to receive benefits or the obligation to absorb losses that could potentially be significant to the VIE, it might be appropriate to refer to "the obligation to absorb losses from an expenditure of financial resources in the case of those parties who are third party service providers or service providers acting in a fiduciary capacity." Mr. Buller stated another problem is that once an investment company has a VIE under the proposed model, the investment company would be the primary beneficiary. Mr. Herz asked why Mr. Buller thought an investment company would have to consolidate under the proposed model. Mr. Roberge asked how Mr. Buller concluded that he had a variable interest based on the company's arrangements. Mr. Buller stated that an investment company might have a variable interest when it is involved with highly leveraged vehicles or for entities where the equity investors do not have kick-out rights.

Issue 2: Separate Classification in Financial Statements

37. Mr. Golden said that some comment letters had mentioned that separate classifications of consolidated variable interests should be permitted but not required. Mr. Janson stated that from the private company perspective, users might have a direct relationship with the preparer as a lender or surety. He said that in these cases, permitting separate classification would be useful because some users might prefer separate classification while others may not. Ms. O'Dell agreed that an option for separate classification of consolidated variable interests would be useful for private company financial statement users because different users have different levels of access to information which might dictate whether users would prefer separate classification.

Issue 3: Scope

38. Mr. Golden stated some comment letters said that the proposed amendments to FIN 46(R) are an improvement, but certain companies should have exceptions. Mr. Golden said that Mr. Tran requested an exception from the scope of the proposed amendments to FIN 46(R) for companies within the scope of FASB

Statement No. 163, *Accounting for Financial Guarantee Insurance Contracts*. Mr. Tran stated that companies in the scope of Statement 163 should be scoped out of the proposed amendments to FIN 46(R) because Statement 163 is the appropriate model for financial guarantors. He said that financial guarantors already have significant disclosures under the FASB Statement No. 5, *Accounting for Contingencies*, and Statement 163 disclosures. Mr. Tran said that he does not feel that the proposed amendments to FIN 46(R) would provide additional information to users of financial statements of financial guarantors. Mr. Roberge asked if financial guarantors have a right to take control of a trust if there are certain events that occur. Mr. Tran said that if there is an event of default, the bondholders rights are given to the financial guarantors.

39. Mr. Kviz said that government sponsored enterprises should be exempt from the scope of the proposed amendments to FIN 46(R). He stated that the government sponsored enterprises already account for the guarantee under FIN 45, and all the loans and securities are already disclosed. He said that government sponsored enterprise structures are different than other securitization structures.

40. Ms. O'Dell said that leasing transactions with related parties should be exempt from the scope of the proposed amendments to FIN 46(R). She said that there is conflicting application of FIN 46(R) in this situation in current practice and some private company preparers are issuing financial statements with a GAAP exception to avoid applying FIN 46(R). Ms. O'Dell stated that there are already related party disclosures which disclose the leasing transaction.

Issue 4: Qualitative Assessment

41. Mr. Golden then moved the discussion to the qualitative model. Mr. Campbell said that he is an investment advisor in the business of managing client assets for a fee. He said that putting the assets and liabilities of a pooled investment vehicle on an investment advisor's financial statements does not provide useful information. He said that very similar vehicles may have different structures which could result in different presentation in the financial statements.

42. Mr. Golden said that there is some concern about potential diversity in practice that may result from the proposed amendments to FIN 46(R). Mr. Barbieri stated that there may be some diversity in practice from the qualitative model because when multiple parties are making decisions, it may be difficult to determine which party has the ability to make the most significant decisions. He said that an enterprise must determine what decisions are the most significant and analyze what is enough to determine if an enterprise has the ability to make enough decisions that would lead an enterprise to consolidate a VIE. Mr. Barbieri stated that more guidance is needed related to shared power and current versus potential power. Mr. Siegel asked whether the quantitative assessment would be necessary. Mr. Barbieri said that he did not think the quantitative assessment is necessary and he is concerned that enterprises may default to a quantitative assessment if it is available. Mr. Finnegan stated that he had a problem with viewing control as being mutually exclusive from the party that has the majority of risks and returns.

43. Ms. Knopf stated that she thinks that a qualitative model with the concept of control in the consolidation analysis is superior to a quantitative model. She said that a strictly quantitative analysis can lead to consolidation when an enterprise has no power. She stated that she would prefer to early adopt the proposed amendments to FIN 46(R).

Issue 5: Reconsideration

44. Mr. Golden then moved the discussion to ongoing assessments of whether an entity is a variable interest entity or a voting interest entity and whether an enterprise is a primary beneficiary of a variable interest entity. Mr. Barbieri said that he is not a proponent of ongoing reassessment of whether an entity is a variable interest entity or a voting interest entity. He said that he would not change paragraph 7 of FIN 46(R). Mr. Barbieri stated that he is concerned that constant reconsideration could lead an operating business to become a variable interest entity because of operating losses. He said that ongoing reassessment

would be a huge burden for companies to constantly reassess entities and provide disclosures.

45. Mr. Barbieri stated that he is in favor of a longer term project to look at both derecognition and consolidation. In the short term, he said that the FASB should eliminate qualified special purpose entities, provide enhanced disclosures, and change the reconsideration events under paragraph 15 of FIN 46(R), which outlines the reconsideration events to determine whether an enterprise is the primary beneficiary of the VIE. Mr. Scoles stated that the issue of having to reassess the entity is problematic, especially for those enterprises that do not have the power to direct matters of the entity. He said that users of financial statements may not care if an enterprise has a voting interest or a variable interest in an entity if the enterprise will never be in a position to become the primary beneficiary of the entity. Mr. Scoles said that performing an ongoing assessment of whether an enterprise is the primary beneficiary of a VIE would not be as burdensome.

46. Mr. Kviz stated that he believed reconsideration should be performed quarterly as opposed to an ongoing reassessment because quarterly reassessment would be much more operational.

47. Mr. Schroeder said that he is bothered by putting entities on an enterprise’s balance sheet and moving entities off an enterprise’s balance sheet from period to period. Mr. Lamont said that this also bothers him. Mr. Barbieri stated that the same problem exists today with voting interest entities. Mr. Lamont stated that constantly reassessing whether or not an enterprise is the primary beneficiary of an entity is probably not problematic, but constant reconsideration of whether an entity is a VIE or a voting interest entity raises some issues. Ms. Seidman stated that some good points have been made about the difficultly of an ongoing reassessment of whether an entity is a VIE or a voting interest entity.

Issue 6: Convergence

48. Mr. Golden then moved the discussion whether the FASB should slow down on the Statement 140 and FIN 46(R) projects so that converged standards related to derecognition and consolidation could be issued by the FASB and IASB. Mr. Barbieri stated that he is concerned about a bias towards consolidation in the current FASB projects and some of the results that could obfuscate core earnings. He said that he would prefer enhanced disclosures. Mr. Barbieri said that there are a number of problems in the FIN 46(R) consolidation model that are not addressed in the current FIN 46(R) project. He stated that users have many problems trying to identity when an entity is a VIE, which is a problem that is seen in substantive businesses as well as financial entities. He said that there are still concerns with how a variable interest is determind and how one deals with interest rate risk, especially in money market funds. Mr. Barbieri stated that rather than trying to fix the problems with FIN 46(R), the FASB and IASB should work together to create a single consolidation standard. He said that some current concerns about transparency could be alleviated through disclosure and the removal of qualified special purpose entities.

49. Mr. Golden asked users about whether it would be appropriate to continue with a FASB-only project on consolidation or whether it would be better to focus on a joint project that might be effective three years later than a FASB-only project. Mr. Waldron said that he would prefer the FASB move forward with its current project because the improvements that are being made will help investors. Mr. Schroeder stated that with the current lull in the financial services industry, now is a good time to get this project done. Mr. Kviz said that it would be very difficult to implement the proposed derecognition and consolidation standards. He said that many of Freddie Mac’s twelve million loans are not on balance sheet and it would not be possible to have the required systems in place to account for these loans under the proposed standards. Mr. Kviz stated that implementing the systems necessary for the proposed derecognition and consolidation standards

will take eighteen months and cost in excess of fifty-five million dollars. He does not see any benefit in implementing the proposed FASB standards and then having to change when the joint projects on derecognition and consolidation are completed in a few years.

50. Mr. Campbell stated that he is concerned that different structures can result in different answers, even when those structures have the same investment objective. Mr. Buller stated that under the proposed model, consolidation will greatly be increased and may not benefit the user.

51. Mr. Johns thinks that it may be better to move forward with a converged consolidation standard. He believes a converged consolidation standard may be able to get done quicker than expected, there are currently not many securitizations taking place in the market, and a substantial number of new transactions will be affected by the proposed amendments to FIN 46(R). Mr. Herz stated that one of the problems with a converged standard on consolidations is that since the IASB model will affect all consolidations, the FASB will also have to deliberate changes to all its consolidation guidance.

52. Mr. Johns said that he has an issue with the proposed definition in paragraph 14A(a) of the proposed amendments to FIN 46(R), which states "the power to direct matters that most significantly impact." He said that "most significantly" does not set a materiality standard and most of the examples suggest that if you have any involvement with servicing then you will have to consolidate the VIE. He asked that there be some sort of materiality standard so that you do not automatically consolidate a VIE which you are servicing. Mr. Johns also stated that "the right to receive benefits **or** the obligation to absorb losses" language in paragraph 14A(b) of the proposed amendments to FIN 46(R) should say "the right to receive benefits **and** the obligation to absorb losses" because in most plain-vanilla securitizations servicers have an equity retained interest that can absorb limited losses, but all other losses are absorbed by investors. He said that he does

not think implementing the proposed standards would increase transparency and will result in clouding and earnings deterioration.

Issue 7: Other Comments

53. Mr. Kviz suggested that requiring consolidation on adoption at a carryover basis instead of at fair value should help increase transparency for credit risk. He also stated that the proposed consolidation model will obfuscate Freddie Mac's hedging because the company does a lot of economic hedging that flows through earnings. Consolidation would eliminate some of the items that the company is economically exposed to. Mr. Golden asked why the consolidation on adoption at fair value versus a carryover basis hurts or helps the distortion of credit risk. Mr. Kviz said that by consolidating at fair value, the credit risk has to be embedded in a fair value mark in loans and a loan loss would not be visible on the enterprise's books anymore. He said that the loan loss reserve against non-performing loans would also be invisible.

54. Ms. O'Dell asked if the Board is considering providing all the examples requested in the comment letters or if there will be more guidance about the qualitative assessment, which may be more helpful. Mr. Linsmeier stated that there has not been a final conclusion about the examples or whether the examples will even be in the final standard. He said that in part, the examples were developed as revisions were made to the proposed amendments to FIN 46(R) to stress test whether the words in the proposed amendment were helpful in letting people make judgments related to the qualitative assessment. Mr. Scoles stated that the examples resulted in an enterprise determining that there are powers to direct activities that are significant, but in some cases those powers are shared. He asked if there is a presumption that every entity has significant powers to direct. Mr. Smith asked Mr. Scoles if he was asking if there are brain dead entities. Mr. Scoles said that it seems to him like there are no brain dead entities under the proposed amendments to FIN 46(R). Mr. Linsmeier said that until the Board has fully deliberated on shared power, he would not be able to fully answer whether

there is always a situation where there are powers to direct that are significant in a VIE, but he does believe that there are powers to direct every VIE because nobody gives away assets that could end up having losses without some ability to manage those losses.

DISCLOSURE FSP

Issue 1: Disclosure Objectives of Interpretation 46R

55. Mr. Golden introduced the topic of the proposed disclosures to Interpretation 46(R) and asked preparers if they had concerns.

56. Mr. Scoles expressed concern over the proposed requirement to disclose alternative judgments that could be made that would result in a different conclusion as to the primary beneficiary of a variable interest entity. He indicated that these judgments are highly complex and the disclosure would be difficult to create because of the many significant decisions made. He noted that during the transition, it will be very difficult to make these determinations in retrospect. He also expressed concern that passive investors would not be able to obtain the information necessary to comply with the requirement. He also questioned the introduction of a lower threshold for aggregation—**useful incremental information**.

57. Mr. Golden asked whether the investors were satisfied with the requirements. Mr. Finnegan indicated that the disclosure of judgments made by preparers is useful in helping financial statement users understand the entity and the risks of the reporting enterprise. Mr. Sondhi noted that the complexity mentioned by Mr. Scoles makes the disclosure more helpful. Mr. Smith noted that the size of the disclosure wouldn't be practical. He also agreed that the sensitivity analysis needs to be improved.

Issue 2: Passive Investments

58. Mr. Golden asked investors whether they would find the proposed disclosure information on passive investments useful. Ms. O'Dell noted that banks generally

indicate that they prefer any additional information. Mr. Janson agreed and said that this was consistent with his observation that many private company investors were satisfied with the current disclosures over related party transactions, consolidation (as currently required by FIN 46(R)), guarantees, and contingencies because the variable interest structures for smaller companies are not generally as complex as financing arrangements. He stated that they are more often leasing structures.

59. Ms. Donoghue commented that there seemed to be a desire to scope out passive investments and expressed concern that part of the issue with qualifying special purpose entities arose out of the difficulty in defining passive investments. She asked what wording would be appropriate. Some participants responded that a passive investor would be an investor that is neither the sponsor nor the servicer. Mr. Finnegan noted that an implicit obligation or contractual support would need to be disclosed as well.

Issue 3: Proscriptive Nature of Disclosures

60. Mr. Golden noted that many comments stated that the disclosures were overly proscriptive. He asked for clarification as to whether the principles or the detailed requirements were at fault. Mr. Scoles stated that the disclosure principles were appropriate. He expressed a concern that preparers would default to the specific disclosure requirements rather than using the principles to frame an overall approach to the framework.

61. Mr. Herz agreed that there may be benefits from providing additional information about passive investments. Mr. Schroeder agreed that there would be additional value from broadening the disclosures.

62. Mr. Buller indicated that there is a timing issue as to when this information becomes available because a partnership may not provide this information until several months after the period has ended. He stated that a lag in reporting material performance fees within the partnership has led to reporting and control issues. Mr. Johns indicated that some of the requirements may be duplicative because credit card companies already disclose managed assets.

Question 4: Effective Date

63. Mr. Golden asked what a company needs to do to comply with the proposals. Some preparers stated they would be able to meet the requirements, but there would be significant resource requirements and it would be difficult. Mr. Johns stated that the system will be difficult and costly to implement. He didn't feel that the cost was prohibitive, but felt that the time required to gather the data would make timely compliance difficult. In response to a question by Ms. Seidman, Mr. Johns stated he felt that removing the requirements to gather information regarding passive investments would not eliminate the difficulty, but would provide a substantial reduction in the complexity of preparing the disclosures.

IASB UPDATE

64. Mr. Teixeira stated that the IASB guidance on consolidation is not segregated between variable and voting interest entities. He gave an example of convertibles, which may provide an indication of control, but they are used as protections to the investors rather than as a practical method of gaining control.