

February 10, 2012

Leslie Seidman, Chairman
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116
Via email: director@fasb.org

RE: File Reference No. 2011-220 *Principal versus Agent Analysis*

Dear Chairman Seidman:

The American Bankers Association (ABA) appreciates the opportunity to comment on the Exposure Draft: *Principal versus Agent Analysis* (ED). ABA brings together banks of all sizes and charters into one association. ABA represents banks of all sizes and charters and is the voice for our nation's \$13 trillion banking industry and its two million employees. The majority of ABA's members are banks with less than \$165 million in assets. ABA's extensive resources enhance the success of the nation's banks and strengthen America's economy and communities. Our members are active in the financial markets as banking institutions, trust companies, and broker/dealers. Therefore, we come with a perspective of both a preparer and user of banking and investment manager financial statements.

In the ED, the Board primarily clarifies how entities determine whether a decision maker is using its power over an entity as a principal or as an agent. This analysis affects the determination of whether the assets of the entity should be consolidated with those of the decision maker. While this guidance will have an impact on the analysis pertaining to many different kinds of entities, it has a significant impact on the analysis of the relationship an investment manager has to its respective investment fund. In other words, conclusions from the analysis could result in an investment manager consolidating the assets and liabilities of the respective investment fund onto the financial statements of the investment manager.

The Board introduces a qualitative analysis that emphasizes review of three specific aspects of the decision maker's relationship to the entity:

1. The rights held by other parties,
2. The compensation to which the decision maker is entitled in accordance with its compensation agreement(s), and
3. The investment manager's exposure to variability of returns from other interests that it holds in the entity.

ABA supports the overall direction the Board is taking by emphasizing practical, qualitative factors. We continue to believe that purpose and design of the entity should be the determinative

factors in the analysis and that the above aspects are factors in evaluating the purpose and design. In this context, we believe this overall approach is both operational and will generally yield financial reporting results that both the Board and users of financial statements will find appropriate. In the vast majority of cases, investors are not interested in analyzing financial statements in which the assets under management are consolidated with the general assets of the investment manager.

Exemption for Money Market Funds is Needed

With this in mind, however, the implementation examples do not address the investment manager of a standard money market fund – one in which a \$1 net asset value is maintained on a daily basis (normally, these funds fall under Rule 2A-7 of the Investment Company Act of 1940). Due to potential implicit support of the fund provided by the investment manager (or a related organization) in order to avoiding “breaking the buck”, we believe many organizations may conclude that they are required to consolidate the assets of the money market fund with those of the investment manager. Even if an investment manager does not explicitly support the fund (contractually defined or historically provided in practice), implicit support may often be considered to exist, as money market funds face the same issue, especially in times of general market illiquidity.

The ED notes that consolidating these assets is not the accounting result that the Board is intending, and we believe it is not one that financial statement users desire. However, the implementation guidance suggested in 810-10-55-3AY through 810-10-55-3BK (i.e., Case F) may lead to such a conclusion, since the liquidity risk assumed by the sponsor in the example is considered an implicit variable interest. Widespread divergence in practice, at best, is likely to result without further guidance.

We understand the challenges of addressing the issue of implicit support of money market funds within the construct of the proposed framework. For example, support for these funds, if ever given, is not often strictly related to variability of returns experienced by the fund, but to temporary illiquidity. Further, it is difficult to imagine, practically speaking, many circumstances in which implicit support would not exist or be perceived to exist by shareholders. With the many changes as to regulation of Rule 2A-7 funds currently being considered by the U.S. Securities and Exchange Commission (SEC), it is also very possible that evaluation within this framework may change once those decisions are made by the SEC. We recommend, therefore, that a specific exception be made for money market and other similar investment funds (those compliant with or that operate in accordance with requirements that are similar to those included in Rule 2A-7 of the Investment Company Act of 1940), as well as a discussion as to why such implicit variable interests are different from those described in the implementation guidance.

A Controlling Financial Interest in a VIE Absorbs Potentially Significant Losses

Topic 810-10-25-38A provides the overall principle in determining whether a reporting entity has a controlling financial interest in a variable interest entity (VIE) and, thus, is the VIE's primary beneficiary. The ED has proposed deleting existing language that would require consideration of a reporting entity's obligation to absorb losses of the VIE that could potentially be significant to the VIE. Instead, the resulting ASU, if approved, would consider whether the obligation absorbs *any* losses. In other words, any obligation to absorb losses, no matter how nominal, results in a variable financial interest.

We understand that the Board wishes to avoid bright-lines, but we also believe that the Board still maintains that a variable interest must be substantive in order to be considered for consolidation. Therefore, we recommend that the existing language requiring the obligation to be potentially significant be maintained and that additional implementation guidance (including examples) be included to distinguish between substantive and nonsubstantive variable financial interests.

Clarify That Certain Variable Interest Entities May Have No Primary Beneficiary

Within the discussion of the Principal Versus Agent Analysis (in proposed Accounting Standards Codification (ASC) Topic 810-10-25-38), it is implied that in each VIE, the analysis will identify specific principals or agents of the VIE. In the cases where power is shared, there may be no primary beneficiary (PB). However, in practice, there exist various VIEs that are truly static in design – the scope of a decision maker's authority (and, thus, the power to direct the activities of the VIE) is strictly limited. Within these VIEs, there is no primary beneficiary because neither party has any practical power.

We believe that, without further clarification within 810-10-25-38, diversity in practice will develop or unnecessary analyses will be performed if it is assumed that power over the activities of the VIE must be held by one of the parties. One may erroneously conclude, for example, that a passive investor retains control over the VIE merely because the managing partner/decision maker acts in an agent capacity. With this in mind, we recommend adding additional language to 810-10-25-38 to clarify that a minimum level of exposure is required in order to qualify as a primary beneficiary. Without this minimum level, further analysis (for example, the principal versus agent analysis) is unnecessary. Not only will this additional wording help clarify practice, but also will be more consistent with the principles within International Financial Reporting Standards.

Certain Rights Should be Determinative Factors in the Principal Versus Agent Analysis

ABA agrees with the proposal to consider substantive rights held by multiple parties when evaluating the decision maker's capacity to use its power over an entity as a principal. This is a significant improvement over the current guidance.

With that in mind, however, we believe that when kick-out rights or participating rights are substantive and are held by a limited number of independent parties, this should be a determinative factor in the analysis, not merely a factor to be considered with other factors. Practically speaking, when those conditions are present – the rights held by others are *substantive* and they are held by a *limited* number of parties who are *independent* – it should be generally understood that the powers of the decision maker are limited to an agency role.

We also understand that the Board has a view that the lack of exercise of certain kick-out rights is an indicator that the rights are not substantive. We disagree with this logic. The existence of these rights has incited behavior that has prevented the holders of the rights from exercising them. Therefore, the fact that the rights have not been exercised as often as the Board would have expected is an indicator of their substantive nature.

Currently, the wording in the proposal leaves too many interpretations, which will result in diversity in practice and also unnecessary additional analyses to be performed. Reconsidering situations when kick-out rights are substantive and including the situation above as an example will provide brief, necessary implementation guidance without going into longer and extended facts and circumstances. Therefore, we recommend that the final ASU include language that explicitly considers this combination of factors as determinative.

Implementation Guidance Should be Streamlined

To assist in effective implementation of the ASU, certain implementation guidance can be improved:

1. Implementation guidance in Topic 810-10-55-37 (which reflects paragraph B22 from Statement No. 167/Interpretation 46(R)) addresses fees paid to decision makers. However, this guidance appears to come close to replicating the statements made in 810-10-25-39 paragraphs I through L, causing confusion in determining the specific practice that must be followed. ABA recommends that these paragraphs be reviewed for consideration for deletion or modification.
2. The additional examples proposed to the implementation guidance (810-10-55) assist in understanding the principal versus agent analysis, whereas the existing examples address the overall analysis as to whether an entity has a controlling financial interest in a VIE. Since the analysis in each example is focused solely on one aspect of the analysis, ABA recommends that each of the examples (both existing and proposed) be amended to provide a more holistic analysis (i.e. both the principal versus agent and the overall

analysis) in the consolidation decision. Such guidance will provide a foundation for better practice and documentation expectations.

Thank you for your attention to these matters and for considering our views. Please feel free to contact me (mgullette@aba.com; 202-663-4986) if you would like to discuss our views.

Sincerely,

A handwritten signature in black ink, appearing to read "Michael L. Gullette". The signature is written in a cursive, flowing style.

Michael L. Gullette