

February 7, 2006

Mr. Lawrence Smith
Director of Technical Application and Implementation Activities
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

Dear Mr. Smith:

In the two years since FIN 46(R) was issued, CPAs and other accountants have worked diligently to gain an understanding of the requirements of FIN 46(R) and how those provisions impact their clients. Practitioners have also worked to explain the requirements to their clients and to help them implement the associated changes. Since FIN 46(R) is now effective for non-public entities, The Michigan Association of CPAs Accounting & Auditing Standards Task Force (the MACPA A&A Task Force) wishes to share some of our observations and concerns based on comments we have received from our membership.

The scope of practice for a significant number of our CPA members does not include providing services to public companies. Consequently, December 31, 2005 is the first year end date for which many CPAs have been helping their clients implement the provisions of FIN 46(R). The MACPA A&A Task Force has received a number of communications from its members regarding the implementation difficulties that their smaller clients are experiencing. Our Task Force wishes to communicate these difficulties to the FASB. The Task Force understands that FIN 46(R) is a complex document that naturally requires significant study prior to implementation.

As noted in FIN No. 46 (R):

“the intent of this interpretation was to achieve more consistent application of consolidation policies to variable interest entities and thus to improve comparability between enterprises engaged in similar activities even if some of those activities are conducted through a variable interest entity.”

Based on anecdotal evidence, the MACPA A&A Task Force believes that the document’s complexity has led to many divergent implementation practices which could undermine the FASB’s original intent to “achieve more consistent application of consolidation practices” and “improve comparability.”

Implementation Difficulties

Understandability of the Standards

1. Expected losses and expected residual returns. Issues related to “obligations to absorb expected losses” and “right to receive expected residual returns” of an entity are complex and can require detailed quantitative and qualitative analysis, for example, net present value computations as outlined under FASB Concepts Statement No. 7, *Using Cash Flow Information and Present Value in Accounting Measurements*. Based on comments we have received, without additional guidance as it relates to circumstances common in very small entities, two similar companies with similar variable interest entities subject to consolidation could apply the measurement principles to those cash flows components in vastly different ways due to different understandings of the concepts by different people. Our task force is aware of the provisions within FIN46(R) that acknowledge, under specified circumstances, that certain provisions might not need to be not be applied when this information is not practical to obtain.
2. Determination of a variable interest entity. In the determination of whether an entity is a variable interest entity (VIE), the interpretation refers to “by design.” For example, one test in determining whether an entity is a VIE is to determine whether “by design, the total equity investment at risk is not sufficient to permit the entity to finance its activities without additional subordinated financial support by any party, including equity holders.” FIN 46(R) also states, “an equity investment at risk of less than 10 percent of the entity’s total assets should not be considered to be sufficient to permit the entity to finance its activities without subordinated financial support...unless the equity investment can be demonstrated to be sufficient.” This again is left to the interpretation of financial statement preparers who could reach different conclusions under similar fact patterns. Our task force is aware that no standard can nor should contemplate every possible scenario, but additional examples for very small companies could be helpful.
3. Determination of primary beneficiary. The issue of “primary beneficiary” also presents confusion. In many situations, the primary beneficiary is obvious; however, there also are many situations where this is not as obvious and different conclusions could result under otherwise similar fact patterns.

It is important to note that two of the members of the FASB Board objected to the issuance of this interpretation, “because it does not clarify a new but critical concept underlying variable interest model.” As documented in FIN 46, these two board members believed a lack of clarity exists surrounding the application of the expected loss/return tests, the gateway in determining whether an entity is a VIE and the key quantitative test for identifying who should consolidate an entity.

The MACPA A&A Task Force has also agreed that, if different conclusions are possible (and perhaps likely) assuming similar facts, one of the key intents of FIN 46(R) might not be achieved with the current guidance.

Emergence of Alternative Implementation Methods

Due to the lack of understanding of the relevance of the Interpretation, many of our members' clients have been seeking alternatives to implementation of the Interpretation. One alternative has been to change the financial statement presentation from a GAAP basis to an other comprehensive basis of accounting, such as an income tax basis. Another alternative has been for clients to accept the reporting of a departure from generally accepted accounting principles in their accountant's report or audit opinion. The MACPA A&A Task Force does not believe the FASB's intent was to dissuade non-public small businesses from presenting GAAP financial statements in order to avoid accountant or auditor report modifications; however, this may be the result.

Cost Benefit Considerations

Although the FASB did consider the cost versus benefit issue during its deliberations, the MACPA A&A Task Force does not believe it was addressed fully as it relates to very small, non-public entities. As a result, our members have found it difficult to explain the benefits of the standard to their clients in a way that justifies the cost of implementation. The MACPA A&A Task Force is aware of the exemption provisions in paragraph 4(g) of the Interpretation. In addition, while various third-party practice aids have emerged to assist financial statement preparers with implementation, the task remains onerous for the smallest entities.

Conclusion and Recommendations

The complexity of the Interpretation is evident by the history of FIN 46(R). The original FIN 46 was revised after the FASB learned that certain provisions of the original Interpretation were not being interpreted as intended. FIN 46(R) attempted to address these technical and implementation issues. The FASB has also released numerous FASB Staff Positions as further clarification. Based upon the number of revisions and clarifications required to date, it may be necessary to revisit the Interpretation, its guidance or methods of implementation.

The MACPA A&A Task Force respectfully requests the FASB consider the following actions:

1. Simplify FIN 46 with regard to non-public entities or exempt small non-public business entities from the consolidation provisions of the Interpretation, but retain expanded disclosure of the information relevant to variable interest entities through existing related party disclosures.
2. Retroactively delay the implementation effective dates for non-public entities until further clarifications are made and guidance for implementation is provided.

The MACPA A&A Task Force consists of a cross section of MACPA members, including members in public practice, education and industry. Our public practice members represent sole practitioners, local firms and regional firms. As part of our process for communicating with standards-setting bodies, we request comments from our task force members and from MACPA members who have expressed an interest in the accounting and auditing area. We consider these

comments when discussing and preparing our task force's comments. The comments in this letter represent our composite views on the issue.

If you have any questions regarding our comments or suggestions for remedies, please contact the MACPA Government Relations & Regulatory Affairs Department at (248) 267-3700. Thank you in advance for your time in considering our concerns.

Sincerely,

A handwritten signature in black ink, appearing to read "Duane M. Reyhl". The signature is fluid and cursive, with the first name "Duane" being the most prominent.

Duane M. Reyhl, CPA
Chair, MACPA Accounting & Auditing Standards Task Force

Cc: Dan Noll, Director – American Institute of CPAs (AICPA) Accounting Standards Team