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February 10, 2012

Ms. Susan M. Cosper
Technical Director
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

By e-mail: director@fasb.org

Re: Proposed Accounting Standards Update –
Financial Services—Investment Companies (Topic 946)
Amendments to the Scope, Measurement, and Disclosure Requirements
(File Reference No. 2011-200)

The New York State Society of Certified Public Accountants (NYSSCPA), representing more than 28,000 CPAs in public practice, industry, government and education, welcomes the opportunity to comment on the above captioned Exposure Draft.

The NYSSCPA's Financial Accounting Standards Committee and Investment Companies Committee deliberated the Exposure Draft and prepared the attached comments. If you would like additional discussion with us, please contact J. Roger Donohue, Chair of the Financial Accounting Standards Committee at (516) 887-7573 or Ernest J. Markezin, NYSSCPA staff at (212) 719-8303.

Sincerely,

NYSSCPA

Richard E. Piluso
President

Attachment

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NEW YORK STATE SOCIETY OF

CERTIFIED PUBLIC ACCOUNTANTS

COMMENTS ON

PROPOSED ACCOUNTING STANDARDS UPDATE – FINANCIAL SERVICES—INVESTMENT COMPANIES (TOPIC 946) AMENDMENTS TO THE SCOPE, MEASUREMENT, AND DISCLOSURE REQUIREMENTS

(FILE REFERENCE NO. 2011-200)

February 10, 2012

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New York State Society of Certified Public Accountants

Comments on

**Proposed Accounting Standards Update –
Financial Services—Investment Companies (Topic 946)
Amendments to the Scope, Measurement, and Disclosure Requirements
(File Reference No. 2011-200)**

We have reviewed the Financial Accounting Standards Board ("FASB") proposed Accounting Standards Update, *Financial Services—Investment Companies (Topic 946) Amendments to the Scope, Measurement, and Disclosure Requirements* (the "Update"), and we appreciate the opportunity to provide our comments and responses to the questions for respondents.

General Comments

We understand that continuing from the development of a revised standard for consolidation, the FASB and the International Accounting Standards Board (IASB) wanted to develop consistent criteria for determining whether an entity is an investment company because investment companies carry all of their investments in operating entities at fair value even if they hold a controlling financial interest in the investee. The proposed Update would amend the guidance in Topic 946 by developing consistent criteria for determining whether an entity is an investment company, and we assume related guidance will be provided in the AICPA's *Investment Companies Audit Guide*.

Overall, we are in agreement in principle with the Board's proposed Update to Topic 946. There are certain aspects of the Update which, in our view, could result in significant changes, possibly unanticipated, to current industry practice and require additional guidance or clarification. The approach with our responses is to provide additional perspective on investment company industry accounting and business issues. We also highlighted areas in which if guidance is issued but not clarified could result in unintended diversity in practice.

As drafted, the proposed criterion regarding consolidation of one investment company by another investment company, pooling of funds and unit of ownership is the topic we would like to have the Board reconsider. There are various types of investment vehicles currently in practice that follow investment company accounting guidance accounting for their investments at fair value and reporting a net asset value or equivalent. These entities would no longer be able to apply investment company accounting because they have a single investor or a group of related investors. In some scenarios, these investors might not issue financial statements in accordance with U.S. GAAP or might not issue financial statements at all. In other scenarios, reporting their investments at fair value by these entities may be required by regulators. A "bright line" test solely based on number of investors or the relationships between investors does not allow for a principles-based approach in which the qualitative aspects, within a framework of the entity and its investors can be considered for determining if the application of Topic 946 is the appropriate reporting framework.

Responses to Specific Questions

Scope

Question 1: The proposed amendments would require an entity to meet all six of the criteria in paragraph 946-10-15-2 to qualify as an investment company. Should an entity be required to meet all six criteria, and do the criteria appropriately identify those entities that should be within the scope of Topic 946 for investment companies? If not, what changes or additional criteria would you propose and why?

Response: In general, the answer is yes. However, some questions have arisen that we feel need to be considered.

We are asking for additional clarification and guidance regarding the last sentence in criteria 946-10-15-2 (d): "The entity can be but does not need to be a legal entity." This criterion appears to be inconsistent with criteria 946-10-15-2 (b) which stipulates unit ownership. "Ownership in the investment company is represented by units of investments, such as shares of stock in the form of equity or partnership interests, to which a portion of the proportionate shares of net assets are attributed." The Master Glossary in the Accounting Standards Codification defines equity interests as; "used broadly to mean ownership interests of investor-owned entities; owner, member, or participant interests of mutual entities; and owner or member interests in the net assets of not-for-profit entities."

If the reporting entity is not a legal entity and does not have a form of legally defined units or partnership interests, it becomes unclear how such unit ownership is determined and evidenced. Additionally, if the reporting entity is not a legal entity it could make management's substantiation of the financial statement assertions of rights, obligations and completeness difficult (if not impossible) as a practical matter depending on the nature of the particular entity. We request that the Board provide additional guidance on these questions.

For example, certain separate accounts of insurance companies are silent and do not specify units or that $1 is the unit. The account is set up similar to partnership ownership. The definition or an example of a unit in a partnership would need to be expanded to include this type of ownership of an insurance company pooled separate account or a comment added that if silent $1 is the assumed unit.

Employee benefit plans invest in separate accounts of insurance companies. These accounts are not separate legal entities but issue financial statements to the investing public. Historically, these pooled separate accounts have provided financial statements, but the assets are not owned by the account. These assets are in the name of the insurance company; and the investor owns a contract with an insurance company that will perform similarly to a specified portfolio of assets. The insurance company increases or decreases the value of the portfolio based upon the performance of those assets. Under the proposed ASU, would these pooled separate accounts continue existing practice or change? Would they be scoped out of the proposed ASU? We request that the Board provide additional clarification.

In addition, we have some questions on the requirement for multiple ownership in order to be treated as an investment company. Currently, endowment funds, universities, not-for-profit organizations and family trusts set up separate funds that do not have other investors. These funds are required to provide financial statements prepared in accordance with U.S. GAAP. In reading this Exposure Draft, it appears that these situations will no longer qualify for Investment Company accounting. Clarification and examples of these situations should be provided. Also, some investment managers have set up brother-sister funds. One fund is for the investors and the other fund invests in the same securities with the same strategy except a different fee structure is set up for employees. If the employees are defined as one related party and not multiple investors, it appears that, in the future, these two funds would be accounted for under different standards if the employees are defined as one related party and not multiple investors. Is this the intent of the standard?

Also, consider the differing investment company structures existing currently and expanding the examples given in the guidance to include these and other similar examples.

Question 2: The definition of an investment company in the proposed amendments includes entities that are regulated under the SEC's Investment Company Act of 1940. Are you aware of any entities that are investment companies under U.S. regulatory requirements that would not meet all of the proposed criteria in paragraph 946-10-15-2? If so, please identify those types of entities and which of the criteria they would not meet.

Response: We are aware of situations in which the SEC requested registrants who have sold an operating business and had not acquired another operating business in more than five years to file as an Investment Company Act of 1940 company (a "1940 Act Company"). One registrant's only assets were cash in the form of a CD and prepaid assets representing less than 1% of total assets. There were accrued expenses and accounts payable representing less than 1% of the total assets. The company was still looking for an operating company to purchase. The articles of incorporation indicate the purpose of the entity was to operate businesses. If the company had not gotten an extension to find a company to purchase or to liquidate and distribute the net assets to its shareholders, it would have been required to file as a1940 Act Company. The company would not have met the proposed criteria to be an Investment Company.

Question 3: The proposed amendments would remove the scope exception in Topic 946 for real estate investment trusts. Instead, a real estate investment trust that

meets the criteria to be an investment property entity under the proposed Update on investment property entities would be excluded from the scope of Topic 946. Do you agree that the scope exception in Topic 946 for real estate investment trusts should be removed? In addition, do the amendments in the proposed Updates on investment companies and investment property entities appropriately identify the population of real estate entities that should be investment companies and investment property entities?

Response: Yes, we agree that the scope exception for real estate investment trusts should be removed. Real estate investment trusts would first be evaluated under the investment property criteria. If the real estate investment trust does not meet the criteria as an investment property entity then the trust should consider whether it meets all six criteria as an investment company. If the six criteria are not met the real estate trust should follow the consolidation guidance.

We feel the examples should be expanded to provide a sample of a real estate trust that would qualify for treatment as an investment company.

Question 4: The proposed amendments would require an entity to reassess whether it is as an investment company if there is a change in the purpose and design of the entity. Is this proposed requirement appropriate and operational? If not, why?

Response: In our view this requirement is appropriate and operational. The change of purpose of design of the entity other than termination would require a change in the prospectus, articles of partnership or incorporation and, in most cases, approval of the investors/unit holders or notification of the investors/ unit holders.

Nature of the Investment Activities

Question 5: An entity may be an investment company when it performs activities that support its investing activities. As a result, a real estate fund or real estate investment trust (that is not an investment property entity) could be an investment company if the entity (directly or indirectly through an agent) manages only its own properties. However, the entity would be precluded from being an investment company if the other activities were considered more than supporting the entity's investment activities (for example, construction). Is this requirement operational, and could it be consistently applied?

Response: Yes, this requirement is operational and could be consistently applied. Only time and practical experience will tell how the words "not substantive" are interpreted. Consideration should be given to providing an example of a scenario in which providing services to other entities would not be substantive without using the words "not substantive" in the example until the conclusion. This requirement will also apply to private equity funds that invest in companies and where management is provided through an entity related to the general partner with the thought of growing, combining, restructuring and then selling the company invested in to another entity or to the public in an initial public offering (IPO).

Question 6: The proposed implementation guidance includes examples of relationships or activities that would indicate that an entity obtains or has the objective of obtaining returns from its investments that are not capital appreciation or investment income. Do you agree with these examples? If not, how would you modify the examples while still addressing the Board's concerns identified in paragraphs BC15 and BC16?

Response: We agree with these examples.

Unit Ownership and Pooling of Funds

Question 7: To be an investment company, the proposed amendments would require an entity to have investors that are not related to the entity's parent (if there is a parent) and those investors, in aggregate, must hold a significant ownership interest in the entity. Is this criterion appropriate? If not, why?

Response: We agree the criterion is appropriate.

Question 8: The proposed unit-ownership criterion would require an entity to have ownership interests in the form of equity or partnership interests to be an investment company. The entity would consider only those interests in determining whether it meets the proposed pooling-of-funds criterion. Therefore, a securitization vehicle, such as a collateralized debt obligation, may not qualify as an investment company under the proposed amendments because it may not meet the unit-ownership or the pooling-of-funds criterion. The entity would not consider interests held by its debt holders when evaluating these criteria to be an investment company. For entities that do not have substantive equity interests (for example, those considered variable interest entities under Subtopic 810-10), should the unit-ownership and pooling-of-funds criteria to be an investment company consider interests held by debt holders? Please explain.

Response: We agree that debt interests held by debt holders should not be considered when evaluating the criteria to be an investment company.

Question 9: Certain entities may meet all of the other criteria to be an investment company yet have only a single investor (for example, a pension plan). The amendments in FASB's proposed Update on investment property entities provides that if the parent of an entity is required to measure its investments at fair value under U.S. GAAP or the parent entity is a not-for-profit entity under Topic 958 that measures its investments at fair value, the entity would not need to meet the unit-ownership and pooling-of-funds criteria to be an investment property entity. Considering the Board's concerns identified in paragraph BC24, should the criteria in this proposed Update be amended to address situations in which the entity has a single investor?

Response: An entity should not be required to have multiple investors as long as it meets the other criteria in order to meet the definition of an investment company. It is common to set up single investor entities in the Industry for a variety of valid business reasons including income tax efficiencies because a single investor wants to segregate its investment, an investor wants to invest a significant amount in a particular strategy or an existing fund is closed and a fund manager has offers of new capital. Many of these investors do not issue U.S. GAAP financial statements. Those investors could be foreign sovereign entities or not-for-profit entities. Certain family trusts may require separate investments for each beneficiary of the trust. Yet, these entities may still need the investee assets and liabilities reported at fair value and the equivalent of NAV.

If, according to paragraph BC 24 of the exposure draft, the reason for this very restrictive pooling of funds criterion is that “the Boards were concerned that without such a requirement, an investment company could be inserted into a larger corporate structure to achieve a particular accounting outcome,” then in our view this criterion is not appropriate. As discussed previously, it is common practice in the Industry to have single investor investment companies or an investment company that has as its equity only a group of related investors. These equity investor(s) in many cases may not be entities or individuals that issue financial statements in accordance with U.S. GAAP. The Board has expressed a valid concern. However, we feel it is a consolidation issue and should be addressed in the consolidation guidance rather than the investment company definition guidance.

In our response to question No. 1, we included an example of a family trust that is silent on the requirement to measure its investments at fair value. The trust documents indicate that the financial statements of the trust are to be prepared in accordance with U.S. GAAP. In the past, the trust has prepared its financial statements measuring its investments at fair value. The trust would meet all of the other requirements of being an investment company. Would this entity meet the exception? Because the members of the family are related, we would assume that the trust would not qualify as having multiple members. Consider adding this scenario as an example.

Pension plans reporting under section 960 which are subject to *The Employee Retirement Income Security Act of 1974* (ERISA) rules are currently required to report at fair value. Please clarify if section 960 will be affected by the changes in investment property, investment companies or principle versus agent.

Question 10: The unit-ownership and pooling-of-funds criteria in the proposed amendments do not consider the nature of the entity’s investors for evaluating if an entity is an investment company. That is, the criteria do not differentiate between passive investors and other types of investors. Do you agree that the nature of the investors should not be considered in evaluating the unit-ownership and pooling-of-funds criteria?

Response: We agree that the nature of the investors should not be considered in evaluating the unity-ownership and pooling-of-funds criteria.

Fair Value Management

Question 11: The proposed amendments would require that substantially all of an investment company's investments are managed, and their performance evaluated, on a fair value basis. Do you agree with this proposal? If not, why? Is this proposed amendment operational and could it be consistently applied? If not, why?

Response: We agree with the proposed amendments. We also think the proposed amendment is operational and could be consistently applied.

Interests in Other Entities

Question 12: The proposed amendments would retain the requirement that an investment company should not consolidate or apply the equity method for an interest in an operating company unless the operating entity provides services to the investment company. However, the proposed amendments would require an investment company to consolidate controlling financial interests in another investment company in a fund-of-funds structure. An investment company would not consolidate controlling financial interests in a master-feeder structure. Do you agree with this proposed requirement for fund-of-funds structures? If not, what method of accounting should be applied and why? Should a feeder fund also consolidate a controlling financial interest in a master fund? Please explain.

Response: The Board should set forth a clear definition of what it means by "controlling financial interests" for consolidation purposes in a fund-of-funds structure. Funds are controlled by the general partner or managing member of their respective partnership or LLC, with few exceptions. Therefore, limited partners or LLC non-managing members of deemed partnerships do not have control over the investment entity in a fund-of-funds structure regardless of percentage ownerships (*i.e.* more than 50%). The only control or influence these limited partners or non-managing members may have over the fund in a fund-of-funds structure would be withdrawal rights. There is usually no other controlling or protective rights associated with these equity interests in a fund-of-funds structure.

Based on the significance of the limited partner's equity ownership interest in the fund–of-funds, additional reporting and disclosure may be necessary in the event there is a "significant financial interest" in the fund. Item BC38 discusses that there was an initial agreement not to consolidate but to add disclosures for a fund-of-funds investment, as the IASB had suggested, but the FASB decided against it because it would result in "an investment company not consolidating 100% owned subsidiaries." If the concern is that these entities may be excluded, the guidance could be amended to include the scenario where a 100% owned subsidiaries should be required to be consolidated (or another scenario in which the fund is truly a subsidiary and that there is truly a controlling interest in the entity–without regard to the financial interest aspect–which is similar to a VIE analysis to be performed by the fund).

There should be an exception, that in the instance of a true fund-of-funds structure, the investment company would apply more of a qualitative analysis to determine if consolidation is appropriate (which is already alluded to in the investment company guide as an optional reporting structure to be considered--Item 5.54 in the 2011AICPA Audit and Accounting Guide, *Investment Companies* or FASB ASC 946-210-45-7) or if investment company accounting should be maintained.

Consideration of the following fact pattern should also be taken into account when the required consolidation in a fund-of-funds structure is being proposed by this exposure draft. There may be a situation in which an investment fund may have a 50% ownership in a fund-of-funds at one reporting period; a 30% ownership during the next reporting period; 20%; 80%, *etc*. These financial interests may all change in the same reporting period or in future years due to other investors/funds redeeming or contributing in different periods and in different amounts than other investors in the fund-of-funds. This situation could dilute or increase one's ownership interest frequently.

As stated earlier, because limited partners or LLC non-managing members of deemed partnerships do not have control over the investment entity, it is misleading to consolidate, deconsolidate, *etc*., strictly based on controlling financial interests. This would be very onerous for the fund to maintain its books and records. These interests (in a fund-of-fund structure) should not be consolidated but instead should be recorded based upon existing Investment Company accounting with additional disclosures when the investment is considered to have a significant financial interest over the fund. Consolidation should only be required once the investment is evaluated as to design and purpose and the qualitative nature of the investment is truly considered a controlling interest with significant influence on the funds operations and business decisions.

We agree that the master fund should not be consolidated by the feeder fund in a master-feeder structure. Paragraph BC37 indicates that there is enough transparency achieved through the current required reporting structure. (Master financial statements are attached to the feeders). Additionally, because ownership interests in the master may fluctuate significantly as a result of contribution and redemption activity by the feeders, there may be a situation in which one would consolidate in one reporting period and might need to deconsolidate a master-feeder depending on changes in the ownership percentages and financial interests owned by the underlying feeders (subscriptions and redemptions between or among feeders). Also, a situation my transpire when a feeder may only own 25% of the master: there would be no transparency at all if the financial statements were not attached and there would not be controlling financial interest to require consolidation. What would the disclosures include in this situation for non-controlling interests? Transparency would be lost for "non-controlling feeder interests in the master." Under current guidance the reporting would show allocations of the master to the feeder and include the master fund financial statement. However, if there is a mini-master structure, we believe consolidation would be required in that situation. With regard to International

Financial Reporting Standards (IFRS), although the attachment of the master fund financial statements is not consistent with IFRS, the investor in the feeder fund would be provided with more information and more detailed disclosure than would be included if the IFRS version was adopted or if the financial statements were consolidated.

Question 13: The proposed amendments would require an investment company to consolidate a controlling financial interest in an investment property entity. Should an investment company be subject to the consolidation requirements for controlling financial interests in an investment property entity? If not, what method of accounting should be applied and why?

Response: We agree that consolidation of an investment property entity should be required in certain situations. However, the additional clarification regarding what is a controlling financial interest in question No. 12 also should be applicable when determining whether or not to consolidate an investment property entity.

Question 14: The proposed amendments would prohibit an investment company from applying the equity method of accounting in Topic 323 to interests in other investment companies and investment property entities. Rather, such interests would be measured at fair value. Do you agree with this proposal? If not, why?

Response: Yes, we agree with this proposal.

Presentation and Disclosure

Question 15: An investment company with a controlling financial interest in a less-than-wholly-owned investment company subsidiary or an investment property entity subsidiary would exclude in its financial highlights amounts attributable to the non-controlling interest. Do you agree that the amounts attributable to the non-controlling interest should be excluded from the calculation of the financial highlights? If not, why?

Response: Yes, we agree that noncontrolling interests should be excluded from the calculation of financial highlights. The investor in the investment company is interested in the financial highlights of their investment; not in the grossed up information that does not reflect the investor’s investment.

Question 16: If an investment company consolidates an investment property entity, the proposed amendments require the investment company to disclose an additional expense ratio that excludes the effects of consolidating its investment property entity subsidiaries from the calculation. Do you agree? If not, why?

Response: We agree with the additional proposed disclosure.

Question 17: Do you agree with the additional proposed disclosures for an investment company? If not, which disclosures do you disagree with, and why? Would you require any additional disclosures and why?

Response: We agree with the additional proposed disclosures.

Retention of Specialized Accounting

Question 18: The proposed amendments would retain the current requirement in U.S. GAAP that a noninvestment company parent should retain the specialized accounting of an investment company subsidiary in consolidation. Do you agree that this requirement should be retained? If not, why?

Response: No, this proposal is inconsistent with IFRS, and will give controlling companies an ability to understate liabilities.

Effective Date and Transition

Question 19: An entity that no longer meets the criteria to be an investment company would apply the proposed amendments as a cumulative-effect adjustment to retained earnings as of the beginning of the period of adoption by calculating the carrying amounts of its investees as though it had always accounted for its investments in conformity with other applicable U.S. GAAP, unless it is not practicable. If not practicable, the entity would apply the proposed amendments as of the beginning of the period of adoption. Do you agree with this proposal? If not, why?

Response: We agree with this proposal.

Question 20: How much time would be necessary to implement the proposed amendments?

Response: Companies should be able to change agreements, obtain required financial statements, modify charts of accounts and put controls in place within one year to eighteen months. However, this amendment should be adopted at the same time as the Real Estate Investment Properties and Principle vs. Agent (Section 810) modifications. The implementation date should be as of the beginning of a fiscal year.

Question 21: The proposed amendments would prohibit early adoption. Should early adoption be permitted? If yes, why?

Response: We agree that early adoption should be prohibited. This would allow for consistency of presentation and eliminate the possibility of confusion by an investor in more than one investment company if he or she receives statements on a different basis.

Nonpublic Entities

Question 22: The proposed amendments would apply to both public and nonpublic entities. Should the proposed amendments apply to nonpublic entities? If not, how should the proposed amendments differ for nonpublic entities and why?

Response: Yes, the proposed amendments should be applied consistently to nonpublic investment companies as well as public investment companies. Nonpublic funds currently include fund of funds, limited partnerships and private equity funds that are held by the public. Although the level of net worth is higher to invest in a nonpublic investment company than a public mutual fund, investors include individuals who have invested proceeds from sales of homes or invested their retirement savings. These individuals may not be sophisticated investors. Creation of two different standards would confuse these and other investors.