

MEMO# 23998

December 7, 2009

FASB Proposal Defers Adviser Consolidation of Funds Advised

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TO: ACCOUNTING/TREASURERS MEMBERS No. 49-09
MONEY MARKET FUNDS ADVISORY COMMITTEE No. 50-09 RE: FASB PROPOSAL DEFERS
ADVISED CONSOLIDATION OF FUNDS ADVISED

The FASB recently released an exposure draft of a proposed accounting standards update (ASU) that would defer the effective date of FAS 167 for certain investment funds. [\[1\]](#) FAS 167 may require an investment adviser to consolidate funds advised for financial reporting purposes under certain circumstances. The ASU would be effective for annual reporting periods beginning after November 15, 2009 and for interim periods within that first annual reporting period. This effective date coincides with the effective date of FAS 167. While the proposed ASU provides an indefinite deferral, we understand that the FASB and the IASB plan to develop, on a joint basis, guidance for consolidation of all entities during 2010.

The ASU is meant to address concerns about the usefulness of investment adviser financial statements if those advisers were required to consolidate certain of the funds they manage. Further, the deferral should enable the FASB to converge GAAP consolidation guidance with standards being developed by the IASB, which differ from FAS 167 in certain respects. Comments on the exposure draft are due to the FASB by January 6, 2010.

Deferral

The ASU would defer application of FAS 167 to an investment adviser's interest in a fund that has the attributes of an investment company as specified in the accounting standards codification or for which it is industry practice to apply financial reporting principles applicable to investment companies. [\[2\]](#) The ASU would not apply in situations in which the

adviser or its related parties has an explicit or implicit obligation to fund actual losses of the fund that could potentially be significant to the fund. Examples of funds that may meet the conditions for deferral include mutual funds, hedge funds, private equity funds, mortgage real estate investment funds, and venture capital funds.

The ASU indicates that the deferral would not apply to securitization entities, asset-backed financing entities, or entities formerly considered qualifying special purpose entities. For example, the deferral would not apply to structured investment vehicles, collateralized debt/loan obligations, commercial paper conduits, credit card securitization structures, residential or commercial mortgage-backed entities, and government-sponsored mortgage entities.

Money Market Funds

The ASU also provides a deferral of FAS 167 to an investment adviser's interest in a fund that is required to comply with, or operates in accordance with, requirements that are similar to those included in Rule 2a-7 of the Investment Company Act of 1940. The exposure draft notes that some have concluded that an adviser's fees represent a "variable interest" in the money market fund as a result of implicit or explicit guarantees to fund credit losses of the fund in situations in which the net asset value decreases to less than \$1.00. Further, that some have also concluded that any funding provided by an adviser creates an implicit guarantee to investors in a money market fund, and any other money market funds it manages, even in situations in which the adviser has no statutory or contractual obligation to provide future funding.

The exposure draft indicates that the Board did not discuss whether it agrees or disagrees with these conclusions. However, because of the restrictive requirements of Rule 2a-7, the Board believes that FAS 167 should not result in advisers having to consolidate money market funds. Consequently, the Board concluded that money market funds should be deferred from FAS 167 until the joint project with the IASB is completed.

Paragraph B22 of FAS 167

Paragraph B22 of FAS 167 as originally adopted contains an exception intended to allow advisers acting in a fiduciary capacity to not consolidate funds managed. That exception provides that fees paid to an adviser or service provider are not variable interests so long as they meet specified criteria. The ASU would amend paragraph B22 to clarify that advisers must consider related parties when assessing the specified criteria.

Disclosures

The ASU would not defer the disclosure requirements in FAS 167. Accordingly, advisers would be required to provide FAS 167 disclosures for all variable interest entities in which they hold a variable interest, including those which qualify for the deferral.

Gregory M. Smith
Director - Operations/Compliance & Fund Accounting

endnotes

[1] The exposure draft Amendments to Statement 167 for Certain Investment Funds is available at the FASB's website at <http://www.fasb.org/cs/ContentServer?c=Page&pagename=FASB%2FPage%2FSectionPage&cid=1175801893139>.

[2] Attributes of an investment company, as described in ASC 946-10-15-2 are: a) investment activity; b) unit ownership; c) pooling of funds; and d) the investment company is the primary reporting entity.

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