ACCT800  SPE Written Assignment (25 Points)

The off-balance sheet financing can take many forms. Most of them involved the use of special purpose entities (SPEs). The examples of off-balance sheet financing include synthetic leases, the securitization of a pool of assets (i.e., mortgage receivables, consumer loans, etc.), and the repo transactions. While the synthetic leases and the securitization require the use of SPEs, the repo transactions do not.

The questions of this assignment are designed to help you: 1) understand the developments of accounting standards with respect to the consolidation of SPEs, and 2) explore the advances/progresses made by the FASB in closing the loopholes in the reporting of off-balance sheet financing. The standards covered in these questions include the pre-Enron standards of ARB 51 (issued in 1959) and SFAS 140 (issued in 2000), the post-Enron standards of FIN 46 (R) (issued in 2003) and SFAS 166 and 167, issued in June 2009 in response to the recent financial crisis.

Before answering the questions, you should read the following papers:

Questions:
1. (3 Points) What are the procedures to securitize receivables using SPEs? You need to describe all parties involved in this process. (see Bens and Monahan, p1023-1026).

2. (3 Points) When an investment bank is used as the sponsor of a SPE for securitization purpose, what is the role/function of this investment bank? What returns does the sponsor receive and what risk does it assume? (see Bens and Monahan, p1023 -1026).

3. (9 points) Prior to the effective of FIN 46 ( R), the SPEs/conduits for securitizations are hardly consolidated by their sponsors or transferors based on the consolidation rules of ARB 51.
   a. Discuss the consolidation criteria under ARB 51.
   b. The qualifying SPE concept was introduced in SFAS 140 and a qualifying SPE is exempt from consolidation. Discuss the equity requirement of a qualifying SPE prior to FIN 46(R) and under FIN 46 (R).
   c. Explain why many sponsors and transferors of SPEs created for securitization purposes can avoid consolidation under ARB 51 and SFAS 140.
d. The variable interest entity concept was introduced in FIN 46 (R). Describe the conditions for a SPE to be a VIE under FIN 46 (R).
e. Explain the determination of the primary beneficiary of a VIE for consolidation purposes under FIN 46 (R).
f. Discuss the impact of FIN 46 (R) on the consolidation of the SPEs (see Soroosh, J. and J.; Ciesielski (2004); Chasteen (2005); Bens and Monahan (2008))

4. (5 Points) Explain how the sponsors (i.e., investment banks) of SPEs restructured their SPEs to avoid consolidation under FIN 46 (R). (see Bens and Monahan, p1048-1051).

5. (5 points) SFAS 166 eliminates the concept of qualifying SPE while SFAS 167 expands the scope of entities subject to the consideration of consolidation. In addition, SFAS 167 replaces the risk-reward model (i.e., a quantitative analysis model) of FIN 46 (R) with a qualitative assessment model in determining the primary beneficiary for consolidation. Discuss the consolidation criteria (or the determination of the primary beneficiary) under SFAS 167 and the reasons underlying the change from the risk-reward model to the qualitative model. (see Medeiros, J. (2010) and A Filomia Aktas, L. (2009)).