

FASB In Focus

Accounting Standards Update—*Development Stage Entities (Topic 915): Elimination of Certain Financial Reporting Requirements, Including an Amendment to Variable Interest Entities Guidance in Topic 810, Consolidations*

On June 10, 2014, the Financial Accounting Standards Board (FASB) issued guidance intended to reduce the overall cost and complexity associated with financial reporting for development stage entities, without reducing the availability of relevant information.

Accounting Standards Update No. 2014-10, *Development Stage Entities (Topic 915): Elimination of Certain Financial Reporting Requirements, Including an*

What is a development stage entity?

A development stage entity is an entity that devotes substantially all of its efforts to establishing a new business.

In a development stage entity, planned principal operations have not started or, if they have started, have produced no significant revenue.

For example, many start-ups or even long-lived organizations that have not yet begun their principal operations or do not have significant revenue would be identified as development stage entities.

Amendment to Variable Interest Entities Guidance in Topic 810, Consolidation, removes all incremental financial reporting requirements from Generally Accepted Accounting Principles (GAAP) for development stage entities, including the removal of Topic 915 from the *FASB Accounting Standards Codification*[®].

In addition, the update:

- Adds an example disclosure in Risks and Uncertainties (Topic 275) to illustrate one way that an entity that has not begun planned principal operations could provide information about the risks and uncertainties related to the company's current activities.
- Removes an exception provided to development stage entities in Consolidations (Topic 810) for determining whether an entity is a variable interest entity—which may change the consolidation analysis, consolidation decision, and disclosure requirements for a company that has an interest in company in the development stage.

A variable interest entity is an entity for which a consolidation assessment is not based on a majority of voting rights.

Background

At its meeting on July 16, 2013, the Private Company Council (PCC) recommended that the FASB add a project to its technical agenda to determine whether the required presentation of inception-to-date information should be amended or eliminated in the financial statements for private development stage entities.

While the PCC originally identified this issue in the context of private development stage entities, FASB staff research found that the issue was relevant for all development stage entities—both public and private.

As a result, the FASB added the project to its agenda and expanded the scope to include both private and public development stage entities.

Why is the FASB issuing this Accounting Standards Update?

Stakeholders have expressed concerns about the cost and limited relevance of the additional presentation and disclosure requirements specific to development stage entities.

Users of financial statements of development stage entities told the Board that they do not find the inception-to-date information relevant to their decision making. In addition, users do not find the required remaining disclosures useful because they do not define development stage entities the way those entities are defined in Topic 915.

The Board's objective in issuing this standard is to improve financial reporting by reducing the cost and complexity associated with the incremental reporting requirements.

How Does the New Guidance Address These Concerns?

Current GAAP requires a development stage entity to present the same basic financial statements and apply the same recognition and measurement rules as established companies. In addition, it requires a development stage entity to present

The Board believes that a single set of consolidation criteria applied by all reporting entities would benefit users of financial statements by providing more relevant and consistent consolidation decisions across all entities.

inception-to-date information about income statement line items, cash flows, and equity transactions.

In this update, elimination of the incremental reporting requirements for development stage entities will reduce costs by eliminating the requirement to report inception-to-date information in the statements of income, cash flows, and shareholder equity.

The Board also believes the changes will simplify the consolidation accounting guidance by removing the differential accounting requirements for development stage entities. As a result of these changes, there no longer will be any accounting or reporting differences in GAAP between development stage entities and other operating entities.

By adding an example disclosure in Risks and Uncertainties (Topic 275), the update will illustrate one way that an entity, which has not begun planned principal operations, could provide information about the risks and uncertainties related to the company's current activities.

The update will also eliminate the exception for development stage entities in Consolidations (Topic 810) of the *FASB Accounting Standards Codification*[®], simplifying GAAP by reducing avoidable complexity in existing accounting literature.

That exception states that a development stage entity is not considered a variable interest entity subject to consolidation if (1) the entity can demonstrate that it has enough equity to finance the activities it is currently engaged

in and (2) the entity's governing documents and contractual arrangements allow additional equity investments.

The amendments provide cost savings for preparers without reducing information relevance to users of financial statements.

Removing this guidance means that all entities will be evaluated for consolidation using the same guidance. It may also affect whether some development stage entities are evaluated as variable interest entities and consolidated in the financial statements of another reporting entity. This would make financial reporting less complex because all organizations would be using the same guidance for consolidations.

How Do These Changes to GAAP Compare with IFRS?

International Financial Reporting Standards (IFRS) currently do not include the concept of a development stage entity and, therefore, do not provide different guidance on presentation or disclosure for entities in the development stage. As such, the amendments in this proposed update would narrow any existing difference between GAAP and IFRS.

Who Is Affected by the Amendments in This Update?

The Standard affects public and private development stage entities. In addition, it could affect whether a different reporting entity that has an interest in a

development stage entity would have to consolidate that entity into its financial statements.

When Will the Amendments in This Update Be Effective?

There are different effective dates for the elimination of the reporting requirements in Topic 915 and for the elimination of the exception in Topic 810. The Board decided to provide additional time for companies to apply the guidance in Topic 810 because, for many, this may be the first time that they will apply the variable interest entity consolidation guidance. Entities affected by the change may need time to perform the variable interest analyses, draft new variable interest disclosures and address issues that may arise if their consolidation decision changes.

For organizations defined as public business entities the presentation and disclosure requirements in Topic 915 will no longer be required starting with the first annual period beginning after December 15, 2014, including interim periods therein. The changes related to the exception for development stage entities in Consolidations (Topic 810) are effective for annual reporting periods beginning after December 15, 2015, including interim periods therein.

For other organizations, the presentation and disclosure requirements in Topic 915 will no longer be required starting with the first annual period beginning after December 15, 2014. Those requirements will no longer be required for interim periods within subsequent annual periods. The

changes related to the exception for development stage entities in Consolidations (Topic 810) are effective for annual reporting periods beginning after December 15, 2016, and for interim periods within subsequent annual periods.

Early application of each of the amendments is permitted for any annual reporting period or interim period for which the entity's financial statements have not yet been issued (public business entities) or made available for issuance (other entities).

The Accounting Standards Update is available at www.fasb.org. ■

For more information on the project, please visit the FASB website at www.fasb.org.

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