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August 3, 2015

Via email to director@fasb.org

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

Re: Investments—Equity Method and Joint Ventures (Topic 323): Simplifying the Equity Method of Accounting (File Reference No. 2015-280) ("the ED")

Dear Ms. Cosper:

We are pleased to provide comments on the Board's proposed simplifications to the equity method of accounting.

We agree with the Board that accounting for basis differences can be complex and that some investors may not be aware of this requirement. As such, we are sympathetic to providing relief for practitioners in this area. However, we question whether eliminating the notion of basis differences altogether is appropriate. We believe there are conceptual and practical challenges to that approach.

Conceptually, preparers and their investors are both interested in assessing the return on an equity method investment. Since an investee's net assets are often wasting, we believe the investor's asset should reflect a similar consumption over time in order to properly assess its returns. In a historical cost model, an initial investment is often consumed over time to generate returns. Further, if an equity method investment is not reduced for the effect of basis differences (or amortization), impairment losses are likely to occur more frequently, which could mislead users. Practically, forecasting whether and when an investment's value will recover in connection with an impairment test can be quite subjective. As such, we believe preparers will spend more time and effort applying the other-than-temporary impairment model under the ED compared to tracking basis differences in the memo accounts under current practice.

Nevertheless, we still believe the current accounting model can be simplified without adversely impacting investors by adopting an amortization approach. Initially, an investor would qualitatively determine whether "substantially all" of the investee's recognized and unrecognized assets are non-wasting. If so, amortization would not be required, although this assertion would need to be reviewed periodically. Otherwise, the investor would determine an appropriate useful life, e.g., based on the predominant wasting asset of the investee, and amortize its investment accordingly.

We believe such an amortization approach has several advantages. First, it would mitigate the conceptual and practical challenges outlined above that would arise from the proposal to cease

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accounting for basis differences. Second, it would make the initial "purchase price allocation" in the memo accounts to quantify individual basis differences under current U.S. GAAP unnecessary, which we believe would solve the majority of the complexity underlying this issue. Third, it would preserve a link to the "one-line" consolidation principle that is currently used in practice to address interpretive questions about equity method accounting that are not specifically addressed in the Codification. We elaborate on these thoughts in the Appendix.

Separately, we agree with the proposal to eliminate the retroactive requirement for equity method accounting when an investment first qualifies for use of the equity method upon an increase in the level of ownership. We see no reason to assume significant influence existed in prior periods, when in fact it did not. We also note adopting a prospective approach is consistent with a "one-line" consolidation principle, since a change to or from consolidation is accounted for prospectively.

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We would be pleased to discuss our comments with the FASB staff. Please direct questions to Adam Brown at (214) 665-0673 or Gautam Goswami at (312) 616-4631.

Very truly yours,

BDO USA, LLP

Appendix

Question 1: Should accounting for the basis difference of equity method investments as if the investment were a consolidated subsidiary be eliminated? Why or why not? Would amortization of the entire basis difference through equity method earnings be preferable? If so, what would be the suggested amortization period?

We agree with the Board that accounting for basis differences can be complex and that investors may not be aware of this requirement. As such, we are sympathetic to providing some form of relief to practitioners in this area. However, we question whether eliminating the notion of basis differences altogether is appropriate. As indicated in our cover letter, we believe there are conceptual and practical challenges to that approach.

Conceptually, preparers and their investors are both interested in assessing the return on an equity method investment. Since an investee's net assets are often wasting or become so, we believe the investor's asset should reflect a similar consumption over time in order to properly assess its returns. In a historical cost model, we believe it could be misleading to suggest none of the initial investment is effectively consumed to generate those returns. Clearly, the investee deploys and may eventually deplete the capital that its investors provided. Further, if an equity method investment is not reduced for the effect of basis differences (or amortization), impairment losses will occur more frequently. This may actually mislead investors. Specifically, an investor often perceives impairment as a lagging indicator of poor performance. Reporting an "impairment" after the ED is finalized might actually reflect the planned consumption of the initial investment in the incorrect accounting period(s). We do not think artificially high earnings followed by more frequent impairments will improve financial reporting.

Practically, forecasting whether an investment's value will recover, and if so, whether it will recover quickly enough to avoid an impairment charge can be quite subjective. As such, we believe preparers are likely to spend more time and effort applying the other-than-temporary impairment model under the ED compared to tracking basis differences in the memo accounts under current practice, which is more mechanical.

Nevertheless, we still believe the current accounting model can be simplified without adversely impacting investors by adopting an amortization approach, similar to the models used for other long-lived assets in Topics 350 and 360.[1] Initially, the investor would qualitatively determine whether "substantially all" of the investee's assets are non-wasting. If so, amortization would not be required, although this assertion would be reviewed periodically. Otherwise, the investor would determine an appropriate useful life, e.g., based on the predominant wasting asset of the investee, and amortize its investment accordingly (which could reduce the asset to zero). As circumstances change, the useful life would be reassessed. If there is no predominant wasting asset, the Board could reconsider whether a default useful life, similar to the private company election for goodwill, should be applied for the amortization period.

We believe such an amortization approach has several advantages. First, it would mitigate the conceptual and practical challenges outlined above that would arise from the proposal to cease accounting for basis differences. Second, it would make the initial "purchase price allocation" in the memo accounts to quantify individual basis differences under current GAAP unnecessary,

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[1] This approach is similar to identifying the "primary asset" under Topic 360 for purposes of impairment testing. It is also similar to determining whether an intangible asset's useful life is "indefinite" or not.

which we believe would solve the majority of the complexity underlying this issue (i.e., estimating the fair value of individual assets at the investee level). Third, it would preserve a link to the "one-line" consolidation principle that is currently used in practice.

We believe the third advantage is equally relevant. While we agree with the Board that there is an important distinction between significant influence and control, we would not abandon the linkage that exists between Topics 323 and 810. Among other things, it provides a framework for addressing interpretive questions about equity method accounting that arise in practice. For example, many practitioners look to Topic 810 when faced with a difference in fiscal periods that creates a "lag." Topic 323 does not prescribe an upper bound on what constitutes an acceptable lag, although it emphasizes the need for a consistent lag each reporting period (323-10-35-6). However, Topic 810 indicates the lag should not be "more than about three months" (810-10-45-12). Similarly, prior to ASU 2013-08, Topic 323 did not address whether an investee's industry-specific accounting should be retained, in which case some practitioners looked to 810-10-25-15.[2] Eliminating the "one-line" consolidation principle[3] might have the unintended effect of creating diversity. In that circumstance, investors will account for interpretive questions related to new equity method investments without the benefit of the "one-line" consolidation principle that has historically been considered in practice.

If the Board does not accept our recommendation that distinguishes between wasting and non-wasting investments, it might reconsider this question as part of its project related to goodwill for public companies. That is, if the Board ultimately decides that goodwill should be amortized, that might suggest more equity method investments should also be amortized in a similar manner.

Question 2: Should the accounting for capitalized interest, which adds to the basis of an entity's equity method investment and is amortized, also be eliminated for equity method investments? Why or why not?

Under our recommended approach, capitalized interest would be part of the cost of the investment, which may or may not be subsequently amortized, depending on the nature of the investee's underlying assets.

Question 3: Should an entity be required to apply the proposed amendments related to accounting for the basis difference on a modified prospective basis as of the effective date? Why or why not?

We agree with a modified prospective transition method, whether for the Board's proposed approach or our suggested amortization approach.

Question 4: Should an entity no longer be required to retroactively adopt the equity method of accounting if an investment qualifies for use of the equity method as a result of an increase in the level of ownership interest? Why or why not?

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[2] We note the ED does not delete the recent addition of 323-10-25-7. This language, and other portions of the text in Topic 323 that are not amended under the ED, including intra-entity eliminations, continues to reflect a "one-line" consolidation premise.
[3] See paragraphs BC8 – BC9 in the basis for conclusions, which effectively rescind "one-line" consolidation.

We agree with the proposal to discontinue the retroactive treatment as a result of an increase in the level of ownership. We see no reason to assume significant influence existed in prior periods, when in fact it did not.

We also note adopting a prospective approach is consistent with a "one-line" consolidation principle, as a change to or from a consolidation model is accounted for prospectively.

Question 5: Should the proposed guidance to eliminate the requirement to retroactively adopt the equity method of accounting be applied prospectively? Why or why not?

We agree with a prospective approach for the same reasons cited by the Board.

Question 6: How much time will be necessary to adopt the amendments in this proposed Update? Should early adoption be permitted? Should the amount of time needed to apply the proposed amendments by entities other than public business entities be different from the amount of time needed by public business entities?

On the surface, it does not appear that significant time would be required to stop accounting for basis differences or to switch to a prospective method to reflect increases in ownership.

However, it is difficult to foresee how much additional time would be required to complete additional impairment analyses, if any, as a result of issuing a final ASU. In addition, since the ED would generally result in higher carrying amounts for equity method investments, this may trigger additional reporting requirements for public companies under Rules 3-09 and 4-08(g) of Regulation S-X.

Accordingly, we would recommend an effective date for periods beginning after 12/15/16, with an option to early adopt.

Question 7: Would the proposed amendments meet the objective of the Simplification Initiative, which is to improve GAAP by reducing cost and complexity while maintaining or improving the usefulness of the information provided to users of financial statements? Why or why not?

Please see our comments above. We believe the ED poses significant unintended consequences, including an increased number of impairment tests, which may occur in inappropriate periods. Other changes in practice might also result from eliminating the "one-line" consolidation principle.