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August 5, 2016

Via email to director@fasb.org

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

Re: Other Income - Gains and Losses from the Derecognition of Nonfinancial Assets (File Reference No. 2016-250)

Dear Ms. Cospers:

We are pleased to provide comments on the Board's proposal to clarify and simplify the accounting for the derecognition of nonfinancial assets. We support the Board's objective to enhance comparability in this area.

We generally agree with the changes proposed in the exposure draft. We also believe certain clarifications of the final amendments would be helpful, as elaborated in the Appendix A to this letter.

In addition, we encourage the Board to finalize the guidance in the Proposed Accounting Standards Update, *Business Combinations (Topic 805): Clarifying the Definition of a Business* in conjunction with, or prior to, finalizing the guidance in this exposure draft. The scope of this exposure draft relies upon the definition of a business, and as such, we believe that finalizing this exposure draft prior to finalizing the definition of a business would result in unnecessary complexity, as further discussed in our responses to the specific questions on which the Board requested feedback.

We would be pleased to discuss our comments with the FASB staff. Please direct questions to Adam Brown at (214) 665-0673 or Angela Newell at (214) 689-5669.

Very truly yours,

A handwritten signature in black ink that reads "BDO USA, LLP". The letters are cursive and somewhat stylized.

BDO USA, LLP

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Appendix A

Question 1: Is the list of transactions that are excluded from Subtopic 610-20 in paragraph 610-20-15-3 complete? If not, please describe what is missing.

We note that real-estate sale-leaseback transactions are excluded from the scope of Subtopic 610-20 by paragraph 15-3(c). We believe the language in that exclusion should be expanded to address all nonfinancial assets subject to sale-leaseback transactions. As currently drafted, the reference to real estate sale-leaseback transactions could be interpreted to mean a sale leaseback of another type of nonfinancial asset, such as an airplane, must satisfy the derecognition guidance in the ED in order to qualify for sale leaseback accounting under ASC 840-40. Since the ED does not propose to amend ASC 840-40 (which currently addresses non real estate sale-leasebacks), we infer that the Board does not intend to change practice in this area prior to the effective date of Topic 842. If our understanding is accurate, a clarification to paragraph 15-3(c) could be made as follows (added text is underlined): “Real estate and non real estate sale-leaseback transactions; see subtopics 360-20- and 840-40 on leases”. A brief statement confirming the Board’s intent on this point in the basis for conclusions of the final amendments would also be helpful.

In addition, we recommend adding leases to the list of excluded transactions in paragraph 610-20-15-3. One might think of a sales-type or direct financing lease as the “derecognition” of the underlying asset by the lessor under Topic 840/Topic 842. Including leases in the list of exclusions in 15-3 will avoid any such misconception.

Lastly, we note there are no proposed amendments to paragraphs 805-50-25-1 or 30-1 with respect to non-cash asset acquisitions. If the Board does not believe noncash consideration given in these circumstances represents a derecognition issue within the scope of this project, we recommend adding those paragraphs to the list of excluded transactions in 610-20-15-3.

Question 2: Do you agree that transfers of all businesses (including real estate businesses) or nonprofit activities should be excluded from the scope of Subtopic 610-20? If not, please describe the types of businesses that should be included in Subtopic 610-20 and how you would define them.

We agree that transfers of all business, including real estate businesses, or nonprofit activities should be excluded from the scope of Subtopic 610-20. We believe that conforming the accounting for real estate businesses with that for other types of businesses would both simplify and improve GAAP.

Question 3: Given that the amendments in this proposed Update would require all businesses to be excluded from Subtopic 610-20, do you have any further comments on the appropriateness or operability of the amendments in the proposed Accounting Standards Update, Business Combinations (Topic 805): Clarifying the Definition of a Business?

We have no additional comments related to the proposed Accounting Standards Update, *Business Combinations (Topic 805): Clarifying the Definition of a Business*. However, given the impact of this proposed Update to the real estate industry, we reiterate our responses to questions 7 and 11 of the proposed Accounting Standards Update, which are attached to this letter in Appendix B. We also recommend that the Board issue a final standard on the definition of a business in conjunction with or prior to finalizing this exposure draft, as indicated in our cover letter.

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Question 4: The scope of Subtopic 610-20 includes in substance nonfinancial assets, which are defined in the Master Glossary and described in paragraphs 610-20-15-4 through 15-10 in this proposed Update. Is it appropriate to include those transactions within the scope of Subtopic 610-20, and would the guidance be operable? If not, why and what other alternatives would you suggest?

Yes, we agree that it is appropriate to include transactions involving in substance nonfinancial assets within the scope of Subtopic 610-20, and agree that the guidance is generally operable. However, refer to our response to Question 8.

In addition, we recommend incorporating a reference to Topic 815 with Topics 320, 321, 323 and 325 among the types of investments that do not constitute a nonfinancial asset under the ASC Master Glossary definition of an "In Substance Nonfinancial Asset."

Question 5: Paragraph 610-20-15-3(k) in this proposed Update excludes subsidiaries that do not have in substance nonfinancial assets entirely from the scope of Subtopic 610-20. Alternatively, the Board could have decided to apply the guidance in paragraph 606-10-15-4 and separate each asset in a subsidiary that is not a business into different derecognition models. Would this alternative approach be operable for partial sales in which the seller retains an interest in the former subsidiary (see also paragraph BC34)? If yes, please provide examples of how this would be applied. If operable, do you support such an approach?

As explained below, separating each asset in a subsidiary that is not a business into different derecognition models may be operable. However, as noted in BC33, we agree with the Board that the deconsolidation model in Topic 810 continues to be appropriate for the relatively infrequent number of transactions of this nature. We also note paragraph 810-10-40-3A(c) requires reporting entities to conclude that the substance of the transaction is not addressed directly by other Topics before applying the deconsolidation model in Topic 810.

With respect to operational and structuring concerns, we note that a transfer could result in a different accounting answer depending on whether the assets sold and liabilities assumed are part of a legal entity or not, especially when the consideration received includes variable (or contingent) consideration. We believe that it may be possible to alleviate this difference by requiring separation of each asset in a subsidiary that is not a business into different derecognition models, which would be consistent with the requirement proposed in paragraph 610-20-15-11 to separate and measure various parts of a contract under multiple Topics.

If the Board chooses to align the derecognition accounting for asset groups and subsidiaries that are not businesses and do not represent an in substance nonfinancial asset, we believe that the guidance in paragraph 610-20-32-5 could be applied to determine the appropriate treatment of any retained interests in the subsidiary. That is, a retained interest could be accounted for as a form of noncash consideration received. However, complications could arise when accounting for variable consideration and the related guidance in Topic 606 compared to the approaches used in practice today when a seller of a subsidiary is entitled to contingent consideration. As a result, we are generally supportive of the Board's proposal to use the deconsolidation model in Topic 810 instead.

Question 6: When transferring an ownership interest in a subsidiary that is an in substance nonfinancial asset, do you agree that the unit of account should be each distinct nonfinancial asset in the subsidiary?

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We agree with the Board's conclusion in paragraph BC47 that control of each nonfinancial asset in a subsidiary will typically transfer simultaneously, and thus it will be infrequent for an entity to apply the guidance on distinct nonfinancial assets. Given the inherent complexity added by allocating the consideration to each distinct nonfinancial asset, we recommend that the Board incorporate the concepts articulated in BC47 into the body of the standard, and indicate that the concept of separating the subsidiary into distinct nonfinancial assets is only applicable if the timing of transfer of control differs for distinct nonfinancial assets.

Question 7: Do you agree that an entity should measure a retained interest in a nonfinancial asset at fair value? If not, why?

Yes, we agree that a retained interest in a nonfinancial asset should be measured at fair value. We agree with the Board's view expressed in paragraph BC67 that the nature of the asset changes in this situation from a nonfinancial asset to a financial asset, and thus measuring it at fair value would be consistent with the accounting for other financial assets.

Question 8: Paragraphs 610-20-40-3 through 40-10 provide guidance that would assist an entity in determining when it transfers control of distinct nonfinancial assets in a subsidiary. Would this guidance be operable? If not, why?

We do not believe that the guidance in paragraphs 610-20-40-3 through 40-10 would be operable for certain transfers of nonfinancial assets and in substance nonfinancial assets. This guidance mandates a two-step process in determining when an entity transfers control. In paragraph 610-20-40-4, an entity must first determine whether it no longer has a controlling financial interest in the subsidiary in accordance with the guidance in Topic 810. Assuming the entity no longer controls the subsidiary, paragraphs 610-20-40-5 through 40-10 then require the entity to determine whether the buyer(s) have obtained control of the asset in the subsidiary. However, in practice, fact patterns exist in which the original owner no longer holds a controlling financial interest in a subsidiary holding a nonfinancial asset, and thus meets the deconsolidation criteria in Topic 810, yet control of the asset has not passed to the buyer(s) under the guidance in 606-10-25-30. Further, neither party expects for control of the building to change hands in the future.

Consider an example. Assume the owner of a building sells 25% of the entity holding the building to a third party. In conjunction with the sale of equity, the owner grants the investor an approval right related to the annual operating budget, which represents a substantive participating right. Under Topic 810, the original owner would no longer be deemed to control the subsidiary, assuming it is a voting interest entity. However, under the guidance in 606-10-25-30, the investor would not be deemed to control the building either. The investor does not have legal title to the asset, nor has physical possession transferred to the investor. In general, the investor has not obtained the significant risks and rewards of ownership because it lacks the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. In this situation, Topic 810 would require the original owner to deconsolidate the entity holding the building without derecognizing the building itself under this ED.

We note case B (paragraphs 610-20-55-20) requires the transferor to record a financial liability in a situation where control didn't transfer due to the presence of a repurchase option. In the basis for conclusions, BC60 appears to articulate a broader principle based on this example by stating, "The Board decided that a reporting entity should recognize a contract liability if the counterparty pays consideration before the entity transfers control of the distinct nonfinancial asset." At a minimum, we recommend incorporating this language into the final amendments to address situations beyond

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the example in Case B. However, we believe constituents will find it counterintuitive to characterize the 25% equity raised in the preceding example as a contract liability. There is no expectation of repayment in cash, nor does either party expect a “contract liability” to be satisfied by transferring the building at some point in the future.

More conceptually, this situation calls into question whether the building continues to meet the definition of an asset under the Concept statements when the reporting entity does not control the entity that owns the asset.

Question 9: Do you agree with providing an entity with the option to apply different transition methods to Subtopic 610-20 and Topic 606? If not, why?

We agree that entities should be allowed to elect different transition methods with respect to Subtopic 610-20 and Topic 606. In addition, we believe that the proposed Update should also allow implementation of Subtopic 610-20 on a prospective basis. Because the types of transfers within the scope of Subtopic 610-20 are by definition not the result of an entity’s ongoing activities, it does not appear that comparability between periods is a key concern for users of the financial statements. In addition, we believe that adoption on a prospective basis alleviates the complexity inherent in question 10 below. We note the FASB’s concerns in BC85 about prospective adoption, but believe this may be addressed by reconsidering the particular disclosure requirements that may be problematic.

Finally, we believe transition efficiencies will be maximized if the Board issues final guidance on the definition of a business in conjunction with or prior to finalizing the guidance in this proposed Update.

Question 10: The proposed amendments on clarifying the definition of a business would require prospective adoption. If those proposed amendments are finalized before Subtopic 610-20 becomes effective, should an entity utilize either:

- a. The definition of a business effective at the time of the transaction***
- b. The revised definition of a business when implementing Subtopic 610-20?***

As discussed above in our response to question 9, we believe that entities should be allowed to implement the provisions of Subtopic 610-20 on a prospective basis, which would alleviate the complexity inherent in this question. However, if the Board declines to provide that election, we believe that an entity should utilize the revised definition of a business when implementing Subtopic 610-20. We believe requiring entities to apply different definitions of a business for different time periods accounted for in a full retrospective or modified retrospective adoption would add unnecessary complexity to the process for little benefit, especially given the non-recurring nature of the transfers within the scope of Subtopic 610-20.

Question 11: Do you agree with the proposed amendments to eliminate the exception in Topic 860 for transfers of equity method investees that were formerly considered in substance nonfinancial assets or in substance real estate? If not, please describe the consequences of applying the guidance in Topic 860 instead of Subtopic 610-20.

We agree with the proposed amendments. We believe that the proposed change will result in consistent accounting treatment for all transfers of equity method investments, which we agree will reduce complexity.

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Question 12: Overall, do you agree that the proposed amendments would reduce the cost and complexity of evaluating the derecognition of nonfinancial assets? Why or why not?

We agree that the proposed amendments would eliminate some of the diversity in practice and complexity of evaluating the derecognition of nonfinancial assets. While this may be partially offset by a more complex definition of what constitutes a business, we believe this represents an acceptable cost.

Other Matters

As a drafting matter, we note that in several places within the proposed amendments, a reference to another paragraph is included instead of reproducing the relevant text itself. We find the heavy reliance on cross-referencing within the proposed amendments challenging to read. In addition, in certain instances, the cross-reference leads a reader to yet another cross-reference, further adding to the difficulty. For example, paragraph 610-20-15-6 directs a reader to paragraph 610-20-15-11 to separate in substance nonfinancial assets in a subsidiary that are within the scope of Subtopic 610 from other parts of the contract. However, paragraph 610-20-15-11 further directs a reader to paragraph 606-10-15-4. Where possible, we believe the readability of the amendments can be improved by using narrative to convey the Board's intent instead of relying on cross-references.

Lastly, we note the proposed amendments will address the investor's accounting for many "joint venture" formation transactions, similar to those contemplated in ASC 970-323. As the Board is aware, there is little authoritative guidance for the receiving entity (i.e., the joint venture) in those circumstances. It is possible that the new guidance provided for investors may influence practice for the recipient entity, something acknowledged by the SEC staff a few years ago.¹ It is difficult to envision whether unintended consequences will result. For instance, a desire to achieve symmetry between the investor and investee may suggest the recipient entity should record noncash assets contributed at fair value. Given the prevalence of these transactions, we encourage the Board to consider a separate project on the investee's accounting for formation transactions.

¹ See the remarks of Josh Forgonne at the 2009 AICPA National Conference on Current SEC and PCAOB developments at <https://www.sec.gov/news/speech/2009/spch120709jsf.htm>: "I'd like to now discuss some interesting questions that have come up concerning the accounting for joint venture formation transactions. However, before we get to the accounting for the joint venture itself, let's spend a minute discussing some of the recent changes to the investor accounting that seems to be driving some of the interest in this topic."

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Appendix B

Responses to selected questions from the proposed Accounting Standards Update, *Business Combinations (Topic 805): Clarifying the Definition of a Business*.

Question 7: The threshold in paragraph 805-10-55-9A also applies to a group of similar identifiable assets. Would the identification of a group of similar identifiable assets be operable? If not, why?

We believe application of the threshold in paragraph 805-10-55-9A to a group of similar identifiable assets is reasonable.

As it applies to commercial real estate, we believe clarification would be helpful regarding whether ground leases (when the acquirer becomes the lessee), which are generally classified as intangible assets, should be combined with or separated from the related leasehold improvements (e.g., buildings and other structures), which are classified as tangible assets. If the ground lease is considered an intangible asset, it appears the ED will reach different conclusions under paragraph 55-9A for the purchase of a building subject to a ground lease compared to the same building being situated on owned property.

Further, we request the Board clarify whether a right-of-use asset under the forthcoming Leases standard will be considered tangible or intangible, and whether a distinction exists between finance and operating leases for this purpose.

Question 11: Do the examples in paragraphs 805-10-55-51 through 55-88 clearly illustrate the application of the proposed guidance? Why or why not?

We agree with the addition of detailed examples to the implementation guidance. . . . In addition, the examples in Case A (paragraphs 805-10-55-52 through 55-55), Case H (805-10-55-76 through 55-83) and Case I (805-10-55-84 through 55-85) help illustrate the application of the proposed guidance with respect to the real estate industry. However, the Board should consider:

- Indicating whether below-market leases should be included in gross assets for purposes of the evaluation in paragraphs 805-10-55-9A through 55-9C. Paragraph 37 of the Basis for Conclusions is clear that the screen is applied with respect to total assets, not to total consideration paid or net assets so that debt (e.g., a mortgage on a building) and “other liabilities” won’t skew the analysis. However, it is unclear why a lease would be treated differently in the analysis based on whether it is above or below market, i.e., whether it represents an asset or a liability.
- Including additional examples in the final guidance given the likely impact on transactions in the real estate industry. For instance, we believe diversity in practice may exist under the current guidance with respect to certain sale-leaseback transactions. An example of a sale-leaseback transaction between an acquirer and an owner-operator (i.e., where no previous lease existed) as well as an example where a seller terminates the existing lease prior to the sale and concurrently enters into a new lease with the acquirer may help to eliminate future diversity in practice in similar transactions.