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Mr. Shayne Kuhaneck
Acting Technical Director
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Re: FASB Agenda Request — Joint venture formation: Initial recognition and measurement for nonmonetary assets [1] contributed by venturers within the financial statements of a joint venture

Dear Mr. Kuhaneck:

Deloitte & Touche LLP appreciates the opportunity to provide an agenda request to the FASB. We request that the FASB consider an agenda topic that would provide additional guidance in Accounting Standards Codification (ASC) Topic 323, *Investments — Equity Method and Joint Ventures*, regarding joint venture formations, specifically, the initial recognition and measurement within the financial statements of a joint venture for nonmonetary assets, including nonmonetary assets that meet the definition of a business in accordance with ASC 805, *Business Combinations*, contributed by venturers.

Background

ASC 323-10-20 provides a definition of a corporate joint venture ("joint venture"). However, the guidance in U.S. GAAP does not address how legal entities that meet the definition of a joint venture should initially recognize and measure, within the financial statements of that joint venture, the nonmonetary assets contributed by venturers upon the joint venture's initial formation.

[1] Including nonmonetary assets that meet the definition of a business under ASC 805, *Business Combinations*.

The Emerging Issues Task Force (EITF) evaluated the accounting by joint ventures for businesses received at the joint venture's formation but did not reach a consensus on this matter.[2] In addition, although ASC 805 provides initial recognition guidance for certain transactions, its scope excludes the formation of a joint venture.

In the absence of guidance from the FASB, the staff of the Securities and Exchange Commission has periodically provided guidance on joint ventures that has influenced the accounting for both private and public entities. At the 1992 AICPA National Conference on Current SEC Developments, Professional Accounting Fellow Steve Blowers stated that the SEC staff would continue to scrutinize any step-up in basis for nonmonetary assets contributed to a joint venture and would permit a full step-up only if all of the following criteria were met:

- Contribution of the asset or business was to a new entity.
- The fair value was objectively determinable and supported by an equal contribution of monetary assets by the other investor(s).
- The monetary assets must have stayed in the new venture or been used for transactions with parties other than the venturers.
- There was an equal allocation of equity and profits or losses between the venturers.
- The new entity was clearly a joint venture; control was shared in meaningful respects (board of directors, shareholder interests, and so forth).

More recently, at the 2009 AICPA Conference on Current SEC and PCAOB Developments, Joshua Forgione, associate chief accountant in the SEC's Office of the Chief Accountant, stated:

> Now, as it relates to the accounting for the joint venture itself, Statement 141(R) excludes from its scope the accounting for the formation of a joint venture. The staff has historically conveyed strong views when considering the use of fair value in recording noncash assets contributed to a joint venture. More specifically, many believe that the staff would only support step-up to fair value when certain conditions are met, including where the asset or business is contributed to a new entity and fair value is supported by an equal amount of monetary assets that either remains in the entity or used by the new entity in transactions with parties other than investors in the venture.
>
> There may be questions developing on the topic of new basis for joint venture formation transactions as a result of these recent changes. The good news or, depending on your perspective, the bad news is that I'm not going to roll out a new model for new basis in joint venture formation transactions. There are certainly a number of good questions surrounding new basis accounting in general. In the absence of additional standard setting, there may be more circumstances where it may be appropriate to record the contributed business at fair value. This is an area that requires a significant amount of analysis and you should carefully evaluate the facts and circumstances surrounding the transaction and determine whether you believe new basis of accounting will result in decision-useful information to investors.

[2] EITF Issue No. 98-4, "Accounting by a Joint Venture for Businesses Received at Its Formation."

In addition to those remarks, there is interpretive guidance from several large accounting firms, with some diversity in views. We also observe that the Board recently acknowledged in ASU 2017-05[3] the need to include guidance from the venturer's perspective on contributions to a joint venture. We believe that standard setting by the Board to provide clarity regarding the issue in this agenda request would improve practice and eliminate diversity.

The appendix to this letter contains a summary of the background of the issue and possible alternatives for the Board to consider in its expansion of the guidance in ASC 323. Because this is a narrow issue that could be resolved in a short time frame, it may best be addressed by the EITF.

We would be happy to share additional perspectives and suggestions with the Board and FASB staff on the matter discussed in our agenda request. If you have any questions concerning this request, please contact Brandon Coleman at 312-486-0259, Michael Morrissey at 203-761-3630, or Andrew Winters at 203-761-3355.

Yours truly,

Deloitte & Touche LLP

cc: Robert Uhl

[3] FASB Accounting Standards Update (ASU) No. 2017-05, *Other Income — Gains and Losses From the Derecognition of Nonfinancial Assets (Subtopic 610-20): Clarifying the Scope of Asset Derecognition Guidance and Accounting for Partial Sales of Nonfinancial Assets.*

Appendix
Deloitte & Touche LLP
Agenda Request — Joint venture formation: Initial recognition and measurement for nonmonetary assets contributed by venturers within the financial statements of a joint venture

Agenda request

This agenda request is limited to the initial recognition and measurement within the financial statements of a joint venture for nonmonetary assets, including nonmonetary assets that meet the definition of a business in accordance with ASC 805, contributed by venturers upon the formation of a joint venture.

Issue

Upon the formation of a joint venture, how should the joint venture initially recognize and measure the contributions of nonmonetary assets within its separate financial statements?

The following three views are potential interpretations of this issue:

- *View A* — Upon formation, a joint venture should initially recognize and measure the contribution of nonmonetary assets at the venturers' carrying amounts in its financial statements.

Proponents of View A do not believe that joint venture formation should reflect a fair-value-based measurement. They make this determination on the premise that in the formation of the joint venture, the venturers who contributed the nonmonetary assets control (albeit jointly) the joint venture. Because the venturer has joint control over the joint venture and thus has not completely surrendered control over the contributed asset(s), a new basis of measurement is not appropriate.

Proponents of View A also look to the guidance in ASC 805-50 on common control transactions. While joint venture formation is not technically within the scope of common control transactions since the venturers, by definition, jointly control the joint venture, proponents of View A believe that joint venture formation transactions are similar to common control transactions. Specifically, proponents of View A believe that under the guidance in ASC 805-50, because there is no change in control, there is no change in the basis of the net assets. ASC 805-50 prescribes that in a common control transaction, the net assets are recorded by the receiving entity at the carrying amounts of the entity transferring the net assets. Proponents of View A believe that the accounting for the joint venture should mirror the guidance in ASC 805-50.

Some View A proponents have also analogized to SAB Topic 5.G (codified in ASC 845-10-S99-1) in analyzing joint venture formation transactions, in which the nonmonetary assets are normally recorded at a historical cost basis (i.e., carrying amounts).

In addition, proponents of View A look to ASC 805, which excludes joint venture formation from the scope of business combination accounting. They argue that if a fair-value-based measurement were appropriate, ASC 805 would not have excluded from its scope, for example, a joint venture's receiving a business upon its formation.

- *View B* — Upon formation, a joint venture should initially recognize and measure the contribution of nonmonetary assets at fair value in its financial statements.

Proponents of View B believe that the initial measurement of nonmonetary assets received by the joint venture upon its formation should be treated no differently than any initial measurement of nonmonetary assets by an entity when received from a third party in a reciprocal exchange.

The general principle in ASC 845, *Nonmonetary Transactions*, is that the exchange is recognized at fair value (i.e., the fair value of the asset surrendered unless the fair value of the asset received is more clearly evident). Proponents of View B observe that ASC 845-10-15-4(b) excludes from its scope "[a] transfer of nonmonetary assets solely . . . between a corporate joint venture and its owners." However, these proponents believe that ASC 845 should be applied by analogy to joint venture formation.

In the case of the formation of the joint venture, the joint venture's acquisition cost for the nonmonetary asset is the fair value of the equity interest exchanged. However, given that the fair value of the nonmonetary asset is generally more reliably measurable than the equity interest of the newly formed entity, the fair value of the nonmonetary asset should be used in the initial measurement.

Proponents of View B also observe that after the remarks made by Mr. Blowers in 1992, the use and requirement of fair-value-based measurement have significantly increased under U.S. GAAP. For example, FAS 141(R),[4] issued in 2007, generally required entities to measure acquired assets and liabilities at fair value in a business combination. In addition, FAS 160[5] was issued in 2007 and required entities to measure retained equity interests at fair value when deconsolidating a subsidiary that meets the definition of a business. In the same year, the FASB issued FAS 157,[6] which defined fair value and established a framework for measuring fair value under U.S. GAAP.

Proponents of View B believe that it is appropriate to analogize to the guidance in ASC 323-10-30-2, which states:

> Except as provided in the following sentence, an investor shall measure an investment in the common stock of an investee (including a joint venture)

[4] FASB Statement No. 141(R), *Business Combinations.*

[5] FASB Statement No. 160, *Noncontrolling Interests in Consolidated Financial Statements*.

[6] FASB Statement No. 157, *Fair Value Measurements.*

initially at cost in accordance with the guidance in Section 805-50-30. **An investor shall initially measure, at fair value, the following**:

a. **A retained investment in the common stock of an investee (including a joint venture**) in a deconsolidation transaction in accordance with paragraphs 810-10-40-3A through 40-5

b. An investment in the common stock of an investee (including a joint venture) recognized upon the derecognition of a distinct nonfinancial asset or distinct in substance nonfinancial asset in accordance with Subtopic 610-20. [Emphasis added]

Proponents of View B argue that the joint venture should apply the same measurement guidance that its venturers follow when they initially contribute nonmonetary assets to a joint venture. These proponents believe that the joint venturer should record the contribution at fair value so that there is no basis difference between the venturers' investments and the joint venture's financial statements.

- *View C* — Upon formation, at their option, joint ventures may initially recognize and measure the contribution of all nonmonetary assets by their venturers at the respective venturers' carrying amounts <u>or</u> at fair value in the joint ventures' financial statements.

Proponents of View C believe that the evolution of pushdown accounting informs the accounting conclusion for the formation of a joint venture. While the accounting in the stand-alone financial statements of a business that has been acquired is not the same as that for the formation of a joint venture, some believe that both are instances in which a new basis of accounting may be reflected. Specifically, an entity that was acquired by a buyer may adjust (or push down) its stand-alone financial statements to reflect the buyer's new basis of accounting by remeasuring its assets and liabilities as of the date of acquisition. Since the issuance of the 1979 AICPA Issues Paper on joint venture accounting,[7] some have argued that the establishment of a joint venture should reflect the new basis for businesses contributed.

While the application of pushdown accounting requires an entity to obtain a controlling financial interest in a business, by definition, a joint venture cannot be controlled by a single entity. Even so, the option provided by ASU 2014-17[8] on pushdown accounting provides evidence of the lack of consensus for the initial measurement of the net assets of an entity that has not been acquired in a business combination. Therefore, proponents of View C believe that the option should be extended to the initial measurement of all nonmonetary assets contributed to a joint venture.

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[7] Paragraph 53a of the 1979 AICPA Issues Paper, "Joint Venture Accounting."

[8] FASB Accounting Standards Update No. 2014-17, *Business Combinations (Topic 805): Pushdown Accounting* — a consensus of the FASB Emerging Issues Task Force.

In summary, View C provides the option for joint ventures to recognize and measure nonmonetary assets received, notwithstanding whether the nonmonetary assets contributed meet the definition of a business.