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Mr. Shayne Kuhaneck
Technical Director
Financial Accounting Standards Board
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Agenda request – Accounting by a Joint Venture for Nonmonetary Assets Contributed by Investors

Dear Mr. Kuhaneck,

I appreciate the opportunity to submit an agenda request to the FASB. I would like the FASB to provide additional guidance in Accounting Standards Codification (ASC) Topic 323, Investments — Equity Method and Joint Ventures, regarding joint venture formations. There is a lack of guidance for the initial recognition and measurement within the financial statements of a joint venture for nonmonetary assets that are contributed. ASC 323, ASC 805 (Business Combinations), and ASC 845 (Nonmonetary Transactions) all fail to specify authoritative guidance on this issue. Due to that lack of guidance, there has been a diversity in the accounting for these type of transactions. I request the FASB eliminate the diversity and improve practice by mandating the use of fair value for these type of transactions.

Background

The accounting guidance for joint ventures falls under the scope of ASC 323. Per ASC 323-10-20, a corporate joint venture is a corporation owned and operated by a small group of entities (the joint venturers) as a separate and specific business or project for the mutual benefit of the members of the group. However, there is no guidance on how a joint venture should initially recognize and measure nonmonetary assets that are contributed by investors. Both ASC 805 (Business Combinations) and ASC 845 (Nonmonetary Transactions) specifically state that the guidance of those topics does not apply to the formation of joint ventures. In the absence of authoritative guidance by the FASB, practice has been diverse and influenced by speeches given by the Securities and Exchange Commission (SEC). This diversity has led to a lack of comparability between similar transactions. Traditionally, there have been two ways to account for these types of transactions. The joint venture would initially account for the nonmonetary assets at either the carry-over value or the fair value.

Issue

How should a joint venture initially recognize and measure nonmonetary assets contributed by investors?

The following two views are acceptable ways to account for this issue. They are both used in practice today.

View A

The joint venture should recognize and measure the nonmonetary assets that are contributed by investors at the carrying value in its financial statements.

Supporters of this view believe that joint venture formations should not reflect the use of fair-value measurement. The venturers who contributed the nonmonetary assets control the joint venture. Since the venturers have joint control over the joint venture, they have not completely given up control of the assets. Therefore, a new measurement of the value of the assets contributed is not appropriate as control has not been transferred.

Per ASC 805-10-15-4, the guidance in the Business Combinations Topic does not apply to any of the following:

- The formation of a joint venture
- The acquisition of an asset or a group of assets that does not constitute a business or a nonprofit activity
- A combination between entities, businesses, or nonprofit activities under common control (see paragraph 805-50-15-6 for examples)

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. Thus, the assets should be recorded at the carry-over value or historical cost.

View B

The joint venture should recognize and measure the nonmonetary assets that are contributed by investors at the fair value in its financial statements.

Supporters of this view believe that the initial measurement of nonmonetary assets received by a joint venture should be similar to that of a business combination/acquisition.

Per ASC 805-10-05-2, the acquirer of the assets should do the following:

- Recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any non-controlling interest in the acquiree
- Recognizes and measures the goodwill acquired in the business combination or a gain from a bargain purchase
- Determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination

As long as a new business entity was formed, the venturers are not related parties, and fair value is readily determinable, the use of fair value to account for these transactions is appropriate. Although ASC 805 states joint ventures are not within the scope, the topic provides the guidance for the use of fair value in business combinations. Supporters argue that nonmonetary assets that are contributed by investors to joint ventures fall in this category.

Recommendation

I would like the FASB to eliminate the diversity in the accounting for these type of transactions by mandating the use of fair value. Upon the formation of a joint venture, nonmonetary assets contributed by investors should be recognized and measured at the fair value of the assets. Any consideration given in excess of fair value should be recorded as goodwill just like the guidance for business combinations in ASC 805. The costs of implementing this change would be minimal. For the most part, fair value measurements are readily determinable. It is rare when fair value measurements are not readily determinable and firms need valuation professionals to assist in the fair value measurements. The benefits of implementing this change would be less diversity among similar transactions improving comparability. Finally, this change would also provide decision-useful information to investors. I believe the use of fair value over carry-over value is superior treatment because it reports more relevant information. Fair value method measures the current situation in the market and reflects more up to date information than the carry-over value method which reflects past transactions and outdated information.

I would be happy to share additional perspectives and suggestions with the Board and FASB staff on the matter discussed in this agenda request. If you have any questions concerning this request, please contact me at 310-283-7563.

Yours truly,

Jay Rama