FINANCIAL ACCOUNTING SERIES

FASB ACCOUNTING STANDARDS UPDATE

No. 2018-17
October 2018

Consolidation (Topic 810)

Targeted Improvements to Related Party Guidance for Variable Interest Entities

An Amendment of the *FASB Accounting Standards Codification*®

Financial Accounting Standards Board

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Summary

Why Is the FASB Issuing This Accounting Standards Update (Update)?

The Board is issuing this Update in response to stakeholders' observations that Topic 810, Consolidation, could be improved in the following areas:

1. Applying the variable interest entity (VIE) guidance to private companies under common control
2. Considering indirect interests held through related parties under common control for determining whether fees paid to decision makers and service providers are variable interests.

The amendments in this Update improve the accounting for those areas, thereby improving general purpose financial reporting.

Who Is Affected by the Amendments in This Update?

The amendments in this Update affect reporting entities that are required to determine whether they should consolidate a legal entity under the guidance within the Variable Interest Entities Subsections of Subtopic 810-10, Consolidation—Overall, including private companies that have elected the accounting alternative for leasing arrangements under common control. The amendments for the private company accounting alternative apply to all entities except for public business entities and not-for-profit entities as defined in the Master Glossary of the *FASB Accounting Standards Codification*® and employee benefit plans within the scope of Topics 960, 962, and 965 on plan accounting.

What Are the Main Provisions?

Private Company Accounting Alternative

Under the amendments in this Update, a private company (reporting entity) may elect not to apply VIE guidance to legal entities under common control (including common control leasing arrangements) if both the parent and the legal entity being evaluated for consolidation are not public business entities.

The accounting alternative provides an accounting policy election that a private company will apply to all current and future legal entities under common control that meet the criteria for applying this alternative. In other words, the alternative cannot be applied to select common control arrangements that meet the criteria for applying this accounting alternative. If the alternative is elected, a private company should continue to apply other consolidation guidance, particularly the voting interest entity guidance, unless another scope exception applies.

Under the accounting alternative, a private company should provide detailed disclosures about its involvement with and exposure to the legal entity under common control.

Effectively, the amendments in this Update expand the private company alternative provided by Accounting Standards Update No. 2014-07, *Consolidation (Topic 810): Applying Variable Interest Entities Guidance to Common Control Leasing Arrangements,* not to apply the VIE guidance to qualifying common control leasing arrangements. Because the private company accounting alternative in this Update applies to all common control arrangements that meet specific criteria and not just leasing arrangements, the amendments in Update 2014-07 are superseded by the amendments in this Update.

Decision-Making Fees

Indirect interests held through related parties in common control arrangements should be considered on a proportional basis for determining whether fees paid to decision makers and service providers are variable interests. This is consistent with how indirect interests held through related parties under common control are considered for determining whether a reporting entity must consolidate a VIE. For example, if a decision maker or service provider owns a 20 percent interest in a related party and that related party owns a 40 percent interest in the legal entity being evaluated, the decision maker's or service provider's indirect interest in the VIE held through the related party under common control should be considered the equivalent of an 8 percent direct interest for determining whether its fees are variable interests.

How Do the Main Provisions Differ from Current Generally Accepted Accounting Principles (GAAP) and Why Are They an Improvement?

Private Company Accounting Alternative

Current GAAP provides a private company with an accounting alternative not to apply VIE guidance to leasing arrangements with entities under common control if certain criteria are met. The amendments in this Update expand the accounting alternative to include all private company common control arrangements if the common control parent and the legal entity being evaluated for consolidation are not public business entities.

This accounting alternative should reduce diversity in applying VIE guidance to private companies under common control because it is expected that many private companies will elect the alternative. This accounting alternative also is expected to improve the relevance of the financial reporting information to users by providing users of private company financial statements with additional disclosures structured in a more consistent manner. Furthermore, the costs and complexity associated with applying VIE guidance to common control arrangements are expected to be reduced for private companies. Therefore, the amendments in this Update meet the overall objective of the *Private Company Decision-Making Framework: A Guide for Evaluating Financial Accounting and Reporting for Private Companies,* for addressing private company stakeholders' needs.

Decision-Making Fees

The amendments in this Update for determining whether a decision-making fee is a variable interest require reporting entities to consider indirect interests held through related parties under common control on a proportional basis rather than as the equivalent of a direct interest in its entirety (as currently required in GAAP). Therefore, these amendments likely will result in more decision makers not having a variable interest through their decision-making arrangements. These amendments also will create alignment between determining whether a decision-making fee is a variable interest and determining whether a reporting entity within a related party group is the primary beneficiary of a VIE.

If fewer decision-making fees are considered variable interests, the focus on determining which party within a related party group under common control may have a controlling financial interest will be shifted to the variable interest holders in the group with more significant economic interests. This will significantly reduce the risk that decision makers with insignificant direct and indirect interests could be deemed the primary beneficiary of a VIE.

The amendments in this Update will increase the consistency of the application of the VIE related party guidance for common control arrangements without compromising the utility of a decision maker's financial statements. Specifically, decision makers that are not determined to be the primary beneficiary of a VIE should provide relevant revenue recognition disclosures under Topic 606, Revenue from Contracts with Customers, when decision-making fees are from contracts that are within the scope of Topic 606.

When Will the Amendments Be Effective?

For entities other than private companies, the amendments in this Update are effective for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years. The amendments in this Update are effective for a private company for fiscal years beginning after December 15, 2020, and interim periods within fiscal years beginning after December 15, 2021. All entities are required to apply the amendments in this Update retrospectively with a cumulative-effect adjustment to retained earnings at the beginning of the earliest period presented. Early adoption is permitted.

Amendments to the *FASB Accounting Standards Codification*®

Summary of Amendments to the Accounting Standards Codification

1. The following table summarizes the amendments to the Accounting Standards Codification. The amendments are organized by area.

Area for Simplification	**Paragraphs**
Issue 1: Private Company Accounting Alternative	3–9
Issue 2: Decision-Making Fees	10 and 11

Introduction

2. The Accounting Standards Codification is amended as described in paragraphs 3–13. In some cases, to put the change in context, not only are the amended paragraphs shown but also the preceding and following paragraphs. Terms from the Master Glossary are in **bold** type. Added text is <u>underlined</u>, and deleted text is ~~struck out~~.

Issue 1: Private Company Accounting Alternative

3. The following amendments reflect the Board's decision to provide private companies with an accounting alternative in applying variable interest entity (VIE) guidance to entities under common control. Because the Board decided to provide this alternative to all private company common control arrangements, it has superseded the amendments in Accounting Standards Update No. 2014-07, *Consolidation (Topic 810): Applying Variable Interest Entities Guidance to Common Control Leasing Arrangements*.

Amendments to Subtopic 810-10

4. Supersede paragraphs 810-10-15-17AA through 15-17C and their related heading, with a link to transition paragraph 810-10-65-9, as follows:

Consolidation—Overall

Scope and Scope Exceptions

Variable Interest Entities

~~**> Accounting Alternative**~~

810-10-15-17AA Paragraph superseded by Accounting Standards Update No. 2018-17.~~Paragraphs 810-10-15-17AB through 15-17C, 810-10-50-2AD through 50-2AF, 810-10-55-9, and 810-10-55-205AJ through 55-205AR provide guidance for an entity electing the accounting alternative in this Subtopic. See paragraph 810-10-65-4 for transition guidance on applying the accounting alternative in this Subtopic.~~

810-10-15-17AB Paragraph superseded by Accounting Standards Update No. 2018-17.~~A **legal entity** need not be evaluated by a **private company** under the guidance in the Variable Interest Entities Subsections if criteria (a) through (c) are met and, in applicable circumstances, criterion (d) is met:~~

~~a. The private company lessee (the reporting entity) and the lessor legal entity are under common control.~~
~~b. The private company lessee has a lease arrangement with the lessor legal entity.~~
~~c. Substantially all activities between the private company lessee and the lessor legal entity are related to leasing activities (including supporting leasing activities) between those two entities.~~
~~d. If the private company lessee explicitly guarantees or provides collateral for any obligation of the lessor legal entity related to the asset leased by the private company, then the principal amount of the obligation at inception of such guarantee or collateral arrangement does not exceed the value of the asset leased by the private company from the lessor legal entity.~~

~~See paragraph 810-10-55-9 and paragraphs 810-10-55-205AJ through 55-205AR for implementation guidance.~~

810-10-15-17B Paragraph superseded by Accounting Standards Update No. 2018-17.~~Application of this accounting alternative is an accounting policy election that shall be applied by a private company to all legal entities, provided that all of the criteria for applying this accounting alternative specified in paragraph 810-10-~~

~~15-17AB are met. For lessor legal entities that as a result of this accounting alternative are excluded from applying the guidance in the Variable Interest Entities Subsections, a private company lessee shall continue to apply other accounting guidance (including guidance in the General Subsections of this Subtopic and guidance included in Subtopic 810-20 on control of partnerships and similar entities) as applicable. A private company that elects this accounting alternative shall disclose the required information specified in paragraph 810-10-50-2AD unless the lessor legal entity is consolidated through accounting guidance other than VIE guidance.~~

810-10-15-17C Paragraph superseded by Accounting Standards Update No. 2018-17.~~If any of the conditions in paragraph 810-10-15-17AB for applying the accounting alternative cease to be met, a private company shall apply the guidance in the Variable Interest Entities Subsections at the date of change on a prospective basis.~~

5. Add paragraphs 810-10-15-17AC through 15-17AF and their related heading, with a link to transition paragraph 810-10-65-9, as follows:

> Accounting Alternative for Entities under Common Control

810-10-15-17AC Paragraphs 810-10-15-17AD through 15-17AF, 810-10-50-2AG through 50-2AI, and 810-10-55-205AU through 55-205BF provide guidance for a **private company** electing the accounting alternative for entities under common control in this Subtopic.

810-10-15-17AD A **legal entity** need not be evaluated by a private company (reporting entity) under the guidance in the Variable Interest Entities Subsections if all of the following criteria are met:

a. The reporting entity and the legal entity are under common control.
b. The reporting entity and the legal entity are not under common control of a **public business entity**.
c. The legal entity under common control is not a public business entity.
d. The reporting entity does not directly or indirectly have a controlling financial interest in the legal entity when considering the General Subsections of this Topic. The Variable Interest Entities Subsections shall not be applied when making this determination.

Applying this accounting alternative is an accounting policy election. If a private company elects to apply this accounting alternative, it shall apply this alternative to all legal entities if criteria (a) through (d) are met. A reporting entity that elects the accounting alternative and, thus, does not apply the guidance in the Variable Interest Entities Subsections shall continue to apply other accounting guidance (including guidance in the General Subsections of this Subtopic) unless another scope exception from this Topic applies. A reporting entity applying this alternative shall disclose the required information specified in paragraphs 810-10-50-2AG through 50-2AI unless the legal entity is consolidated by the reporting entity through accounting guidance other than VIE guidance.

810-10-15-17AE To determine whether the private company (reporting entity) and the legal entity are under common control of a parent solely for the purpose of applying paragraph 810-10-15-17AD(a), the private company shall consider only the parent's direct and indirect voting interest in the private company and the legal entity. In other words, only the guidance in the General Subsections of this Topic shall be considered for determining whether a parent has a direct or indirect controlling financial interest in the private company and the legal entity as required in paragraph 810-10-15-17AD(a). The guidance in the Variable Interest Entities Subsections of this Topic shall not be applied for making this determination. See paragraphs 810-10-55-205AU through 55-205AZ for illustrative guidance.

810-10-15-17AF If any of the criteria in paragraph 810-10-15-17AD for applying the accounting alternative cease to be met, a private company shall apply the guidance in the Variable Interest Entities Subsections at the date of change on a prospective basis, except for situations in which a reporting entity becomes a public business entity. When a reporting entity becomes a public business entity, it shall apply the guidance in the Variable Interest Entities Subsections in accordance with Topic 250 on accounting changes and error corrections.

6. Supersede paragraphs 810-10-50-2AD through 50-2AF and their related heading, with a link to transition paragraph 810-10-65-9, as follows:

Disclosure

Variable Interest Entities

~~> Accounting Alternative~~

810-10-50-2AD Paragraph superseded by Accounting Standards Update No. 2018-17.~~A **private company lessee** that does not apply the requirements of the Variable Interest Entities Subsections to one or more **lessor legal entities** because it meets the criteria in paragraph 810-10-15-17AB shall disclose the following:~~

- ~~a. The amount and key terms of liabilities (for example, debt, environmental liabilities, and asset retirement obligations) recognized by the lessor legal entity that expose the private company lessee to providing financial support to the legal entity. For example, a private company lessee exposed to debt of the legal entity should disclose information such as~~

~~the amount of debt, interest rate, maturity, pledged collateral, and guarantees associated with the debt.~~

~~b. A qualitative description of circumstances (for example, certain commitments and contingencies) not recognized in the financial statements of the lessor legal entity that expose the private company lessee to providing financial support to the legal entity.~~

810-10-50-2AE <u>Paragraph superseded by Accounting Standards Update No. 2018-17.</u>~~In applying the disclosure guidance in paragraph 810-10-50-2AD, a private company lessee shall consider exposures through implicit guarantees. The determination as to whether an implicit guarantee exists is based on facts and circumstances. Those facts and circumstances include, but are not limited to, whether:~~

~~a. There is an economic incentive for the private company lessee to act as a guarantor or to make funds available.~~
~~b. Such actions have happened in similar situations in the past.~~
~~c. The private company lessee acting as a guarantor or making funds available would be considered a conflict of interest or illegal.~~

810-10-50-2AF <u>Paragraph superseded by Accounting Standards Update No. 2018-17.</u>~~In disclosing information about the lessor legal entity, a private company lessee shall present the disclosures in combination with the disclosures required by other guidance (for example, in Topics 460 on guarantees, 850 on related party disclosures, and 842 on leases). Those disclosures could be combined in a single note or by including cross-references within the notes to financial statements.~~

7. Add paragraphs 810-10-50-2AG through 50-2AI and their related heading, with a link to transition paragraph 810-10-65-9, as follows:

<u>**> Accounting Alternative for Entities under Common Control**</u>

<u>**810-10-50-2AG** A reporting entity that neither consolidates nor applies the requirements of the Variable Interest Entities Subsections to a **legal entity** under common control because it meets the criteria in paragraph 810-10-15-17AD shall disclose the following:</u>

<u>a. The nature and risks associated with a reporting entity's involvement with the legal entity under common control.</u>
<u>b. How a reporting entity's involvement with the legal entity under common control affects the reporting entity's financial position, financial performance, and cash flows.</u>
<u>c. The carrying amounts and classification of the assets and liabilities in the reporting entity's statement of financial position resulting from its involvement with the legal entity under common control.</u>

d. The reporting entity's maximum exposure to loss resulting from its involvement with the legal entity under common control. If the reporting entity's maximum exposure to loss resulting from its involvement with the legal entity under common control cannot be quantified, that fact shall be disclosed.
e. If the reporting entity's maximum exposure to loss (as required by (d)) exceeds the carrying amount of the assets and liabilities as described in (c), qualitative and quantitative information to allow users of financial statements to understand the excess exposure. That information shall include, but is not limited to, the terms of the arrangements, considering both explicit and implicit arrangements, that could require the reporting entity to provide financial support (for example, implicit guarantee to fund losses) to the legal entity under common control, including events or circumstances that could expose the reporting entity to a loss.

810-10-50-2AH In applying the disclosure guidance in paragraph 810-10-50-2AG(d) through (e), a reporting entity under common control shall consider exposures through implicit guarantees. Determining whether an implicit guarantee exists is based on facts and circumstances. Those facts and circumstances include, but are not limited to, whether:

a. The **private company** (reporting entity) has an economic incentive to act as a guarantor or to make funds available.
b. The private company (reporting entity) has acted as a guarantor for or made funds available to the legal entity in the past.

810-10-50-2AI In disclosing information about the legal entity under common control, a private company (reporting entity) shall present these disclosures in addition to the disclosures required by other guidance (for example, in Topics 460 on guarantees, Topic 850 on related party disclosures, and Topic 842 on **leases**). Those disclosures could be combined in a single note or by including cross-references within the notes to financial statements.

8. Supersede paragraphs 810-10-55-9 and 810-10-55-205AJ through 55-205AR and their related headings, with a link to transition paragraph 810-10-65-9, as follows:

Implementation Guidance and Illustrations

Variable Interest Entities

> Implementation Guidance

~~> > Accounting Alternative~~

810-10-55-9 Paragraph superseded by Accounting Standards Update No. 2018-17.~~In applying the guidance in paragraph 810-10-15-17AB, the following are examples of activities that are considered to be leasing activities (including supporting leasing activities) between a private company lessee and a lessor **legal entity**:~~

~~a. A guarantee or collateral provided by the **private company** lessee to the lender of a lessor legal entity under common control for indebtedness that is secured by the asset(s) leased by the private company lessee~~
~~b. A joint and several liability arrangement for indebtedness of the lessor legal entity, for which the private company lessee is one of the obligors, that is secured by the asset(s) leased by the private company lessee~~
~~c. Paying property taxes, negotiating the financing, and maintaining the asset(s) leased by the private company lessee~~
~~d. Paying income taxes of the lessor legal entity when the only asset owned by the lessor legal entity is being leased either by only the private company or by both the private company lessee and an unrelated party.~~

~~Paying income taxes of the lessor legal entity on income generated by an asset that is not being leased by the private company lessee is not considered to be a leasing activity between the private company lessee and the lessor legal entity. A purchase commitment (other than for the acquisition of or the support of the leased asset) is not considered to be related to the leasing activity between the private company lessee and the lessor legal entity.~~

> Illustrations

~~**> > Accounting Alternative**~~

~~**> > > Private Company Accounting Alternative for Leasing Arrangements under Common Control**~~

810-10-55-205AJ Paragraph superseded by Accounting Standards Update No. 2018-17.~~The following Examples illustrate the application of the guidance in paragraph 810-10-15-17AB on determining whether a reporting entity that is a private company can elect the accounting alternative not to apply VIE guidance to a legal entity under common control:~~

~~a. Common control leasing arrangement with no leasing or other activities with unrelated parties (Example 6)~~
~~b. Common control leasing arrangement with additional leasing activities with unrelated parties (Example 7)~~
~~c. Common control leasing arrangement with additional activities other than leasing or for the support of leasing (Example 8).~~

810-10-55-205AK Paragraph superseded by Accounting Standards Update No. 2018-17.~~Examples 6 through 8 share all of the following assumptions:~~

~~a. The sole owner of Manufacturing Entity (a private company) is also the sole owner of Lessor Entity.~~
~~b. Manufacturing Entity has pledged its assets as collateral for Lessor Entity's mortgage.~~
~~c. The common owner of both entities has provided a guarantee of Lessor Entity's mortgage as required by the lender.~~
~~d. Manufacturing Entity leases its manufacturing facility from Lessor Entity.~~
~~e. The value of the manufacturing facility leased by Manufacturing Entity exceeds the principal amount of Lessor Entity's mortgage at inception of the mortgage.~~
~~f. Manufacturing Entity has elected to apply the accounting alternative described in paragraph 810-10-15-17AB~~.

~~> > > > Example 6: Common Control Leasing Arrangement with No Leasing or Other Activities with Unrelated Parties~~

810-10-55-205AL Paragraph superseded by Accounting Standards Update No. 2018-17.~~Lessor Entity owns no assets other than the manufacturing facility being leased to Manufacturing Entity. Manufacturing Entity pays property taxes on behalf of Lessor Entity and maintains the manufacturing facility. Therefore, Manufacturing Entity meets all four criteria in paragraph 810-10-15-17AB and, as a result of its elected accounting policy, would apply the accounting alternative to Lessor Entity based on the following:~~

~~a. Manufacturing Entity and Lessor Entity are under common control.~~
~~b. Manufacturing Entity has a lease arrangement with Lessor Entity.~~
~~c. Substantially all the activities between Manufacturing Entity and Lessor Entity are related to the lease of the manufacturing facility to Manufacturing Entity. Providing collateral, paying property taxes, and maintaining the manufacturing facility are considered to be leasing activities between Manufacturing Entity and Lessor Entity as described in paragraph 810-10-55-9.~~
~~d. The value of the manufacturing facility leased by Manufacturing Entity exceeds the principal amount of Lessor Entity's mortgage at inception of the mortgage.~~

810-10-55-205AM Paragraph superseded by Accounting Standards Update No. 2018-17.~~If in two years the value of the manufacturing facility declines below the principal amount of the mortgage, Manufacturing Entity would continue to apply this accounting alternative (assuming no other changes have occurred) because the manufacturing facility met criterion (d) in paragraph 810-10-15-17AB at inception of the arrangement.~~

810-10-55-205AN Paragraph superseded by Accounting Standards Update No. 2018-17.~~If Lessor Entity refinances or enters into a new obligation that requires collateralization or a guarantee by Manufacturing Entity, then Manufacturing Entity would be required to reassess whether criterion (d) in paragraph 810-10-15-17AB is met at the inception of the new obligation. For example, if Lessor Entity refinances the mortgage (collateralized by assets of Manufacturing Entity) and the new principal balance of the mortgage exceeds the value of the manufacturing facility, then the arrangement would no longer meet criterion (d). Not meeting the criteria to qualify for the accounting alternative does not automatically result in consolidation. Instead, Lessor Entity will need to be evaluated under this Topic, including VIE guidance, for consolidation and related disclosure requirements.~~

~~**> > > > Example 7: Common Control Leasing Arrangement with Additional Leasing Activities with Unrelated Parties**~~

810-10-55-205AO Paragraph superseded by Accounting Standards Update No. 2018-17.~~Manufacturing Entity leases 3 of the 10 floors of the manufacturing facility from Lessor Entity. Lessor Entity leases the remaining seven floors of the same manufacturing facility to unrelated parties. Manufacturing Entity continues to pledge its assets as collateral for the mortgage that financed the purchase of the entire manufacturing facility (that is, all 10 floors). In this Example, Manufacturing Entity meets all four criteria in paragraph 810-10-15-17AB and, as a result of its elected accounting policy, would apply the accounting alternative to Lessor Entity based on the following:~~

- ~~a. Manufacturing Entity and Lessor Entity are under common control.~~
- ~~b. Manufacturing Entity has a lease arrangement with Lessor Entity.~~
- ~~c. Substantially all the activities between Manufacturing Entity and Lessor Entity are related to the lease of the manufacturing facility to Manufacturing Entity, even though part of the manufacturing facility is also leased to unrelated parties.~~
- ~~d. The value of the manufacturing facility leased by Manufacturing Entity exceeds the principal amount of Lessor Entity's mortgage at inception of the mortgage.~~

810-10-55-205AP Paragraph superseded by Accounting Standards Update No. 2018-17.~~Subsequently, Lessor Entity purchases an additional facility that is leased only to unrelated parties. The value of the new facility is significant to Lessor Entity, and the mortgage on the additional facility requires a guarantee by Manufacturing Entity. Under these circumstances, Manufacturing Entity failed to meet criterion (c) in paragraph 810-10-15-17AB to qualify for the accounting alternative when the guarantee is executed and leasing activity with unrelated parties commenced. Manufacturing Entity is engaging in substantial activity outside its leasing activity with Lessor Entity by providing a guarantee on a mortgage secured by an asset that is not being leased by Manufacturing Entity. Not meeting the criteria to qualify for the accounting alternative does not automatically result in consolidation.~~

~~Instead, Lessor Entity will need to be evaluated under this Topic, including VIE guidance, for consolidation and related disclosure requirements.~~

~~> > > > Example 8: Common Control Leasing Arrangement with Additional Activities Other Than Leasing or for the Support of Leasing~~

810-10-55-205AQ <u>Paragraph superseded by Accounting Standards Update No. 2018-17.</u>~~Lessor Entity manufactures cosmetics products in another facility that is unrelated to the operations of Manufacturing Entity. There is no mortgage associated with this additional facility, and Manufacturing Entity does not provide collateral or guarantee any obligations related to the cosmetics business. In this Example, Manufacturing Entity meets all four criteria in paragraph 810-10-15-17AB and, as a result of its elected accounting policy, would apply the accounting alternative to Lessor Entity based on the following:~~

- ~~a. Manufacturing Entity and Lessor Entity are under common control.~~
- ~~b. Manufacturing Entity has a lease arrangement with Lessor Entity.~~
- ~~c. Substantially all the activities between Manufacturing Entity and Lessor Entity are related to the lease of the manufacturing facility to Manufacturing Entity.~~
- ~~d. The value of the manufacturing facility leased by Manufacturing Entity exceeds the principal amount of Lessor Entity's mortgage at inception of the mortgage. There is no obligation associated with the purchase of the cosmetic facility.~~

810-10-55-205AR <u>Paragraph superseded by Accounting Standards Update No. 2018-17.</u>~~If there is a mortgage on Lessor Entity's cosmetics facility that requires Manufacturing Entity to provide collateral and/or a guarantee, then Manufacturing Entity may not apply this accounting alternative to the Lessor Entity because it would not meet criterion (c) in paragraph 810-10-15-17AB. A purchase of cosmetics from Lessor Entity by Manufacturing Entity also would require an evaluation of whether criterion (c) of paragraph 810-10-15-17AB is met. Not meeting the criteria to qualify for the accounting alternative does not automatically result in consolidation. Instead, Lessor Entity will need to be evaluated under this Topic, including VIE guidance, for consolidation and related disclosure requirements.~~

9. Add paragraphs 810-10-55-205AU through 55-205BF and their related headings, with a link to transition paragraph 810-10-65-9, as follows:

> > Accounting Alternative for Entities under Common Control

> > > Accounting Alternative—Determining Whether Common Control Exists

810-10-55-205AU The following Examples illustrate the application of the guidance in paragraphs 810-10-15-17AD(a) and 810-10-15-17AE on determining whether common control exists solely for purposes of applying the accounting alternative:

a. Accounting Alternative—Common Control Exists (Example 11)
b. Accounting Alternative—Common Control Does Not Exist (Example 12).

> > > > Example 11: Accounting Alternative—Common Control Exists

810-10-55-205AV Assume the following:

a. Entities A (Parent), B (the reporting entity), C (a legal entity), and E (a legal entity) are all private companies.
b. Entity A holds a majority of the voting shares of Entities B and C.
c. Entity C holds a majority of the voting shares of Entity E.

810-10-55-205AW Based on the guidance in paragraph 810-10-25-1, Entity A has a controlling financial interest in Entities B and C because it directly holds a majority of the voting shares in those entities and no circumstances indicate that control does not rest with the majority owner. Entity C also has a controlling financial interest in Entity E because it directly holds a majority of the voting shares in this entity. Therefore, Entity A controls Entity E through Entity C's controlling financial interest in Entity E. For the purposes of applying paragraph 810-10-15-17AD(a), Entities B, C, and E are under common control of Entity A. Assuming the other criteria in paragraph 810-10-15-17AD are met, Entity B (the reporting entity) is eligible to apply the accounting alternative to Entity C and Entity E.

810-10-55-205AX If Entity B directly holds a majority of the voting shares of Entity E and no circumstances indicate that control does not rest with the majority owner, Entity B would not be able to apply the accounting alternative to Entity E because paragraph 810-10-15-17AD(d) would not be met. In other words, Entity B would conclude that it holds a controlling financial interest in Entity E when considering only the General Subsections of this Topic (and not the Variable Interest Entities Subsections).

> > > > Example 12: Accounting Alternative—Common Control Does Not Exist

810-10-55-205AY Assume the following:

a. Entities A (Parent), B (the reporting entity), C (a legal entity), and E (a legal entity) are all private companies.
b. Entity A holds a majority of the voting shares of Entities B and C.
c. Entities A, B, and C do not hold any voting shares of Entity E (directly or indirectly). However, Entity A has extended subordinated financial support (in the form of debt) to Entity E.

810-10-55-205AZ Based on the guidance in paragraph 810-10-25-1, Entity A has a controlling financial interest in Entities B and C because it directly holds a majority of the voting shares in those entities and no circumstances indicate that control does not rest with the majority owner. Therefore, Entities B and C are under common control of Entity A. However, Entity E is not considered to be under common control of Entity A for the purposes of applying paragraph 810-10-15-17AD(a) because Entity A does not directly or indirectly hold a majority of Entity E's voting shares. Moreover, even if Entity E is a VIE and Entity A is its primary beneficiary, Entity E is not considered to be under common control of Entity A for purposes of applying the guidance in paragraph 810-10-15-17AD(a). Accordingly, Entity B (the reporting entity) is precluded from applying the accounting alternative to Entity E.

> > > Application of the Accounting Alternative

810-10-55-205BA The following Examples illustrate the application of the guidance in paragraph 810-10-15-17AD on determining whether a reporting entity that is a private company can elect the accounting alternative not to apply VIE guidance to a legal entity under common control:

a. Common control leasing arrangement (Example 13)
b. Car Company (reporting entity) under common control with Engine Company, Tire Company, and Purse Company (Example 14).

> > > > Example 13: Common Control Leasing Arrangement

810-10-55-205BB Assume the following:

a. The sole owner (not a public business entity) of Manufacturing Entity (a private company) also is the sole owner of Lessor Entity (a private company).
b. The reporting entity is Manufacturing Entity.

c. Manufacturing Entity leases its manufacturing facility from Lessor Entity.
d. Lessor Entity owns no assets other than the manufacturing facility being leased to Manufacturing Entity.
e. Manufacturing Entity pays property taxes on behalf of Lessor Entity and maintains the manufacturing facility.
f. The sole owner of both entities has provided a guarantee of Lessor Entity's mortgage as required by the external lender.
g. Manufacturing Entity has elected to apply the accounting alternative described in paragraph 810-10-15-17AD.

810-10-55-205BC Manufacturing Entity meets all the criteria in paragraph 810-10-15-17AD, and, as a result of its elected accounting policy, Manufacturing Entity would apply the accounting alternative to Lessor Entity on the basis of the following:

a. Manufacturing Entity (a private company) and Lessor Entity are under common control.
b. Manufacturing Entity and Lessor Entity are under common control of an individual that is not a public business entity.
c. Lessor Entity is not a public business entity.
d. Manufacturing Entity does not directly or indirectly hold a controlling financial interest in Lessor Entity when considering only the General Subsections of this Topic.

Manufacturing Entity should disclose the required information specified in paragraphs 810-10-50-2AG through 50-2AI unless Lessor Entity is consolidated through accounting guidance other than VIE guidance.

> > > > Example 14: Car Company (Reporting Entity) under Common Control with Engine Company, Tire Company, and Purse Company

810-10-55-205BD Assume the following:

a. Reporting entity Car Company (Car Co.), a private company, produces vehicles for sale.
b. Car Co. has elected to apply the accounting alternative described in paragraph 810-10-15-17AD.
c. The sole owner (not a public business entity) of Car Co. also is the sole owner of Engine Company (Engine Co.), Tire Company (Tire Co.), and Purse Company (Purse Co.). Therefore, Car Co., Engine Co., Tire Co., and Purse Co. are considered to be under common control. Only Purse Co. meets the definition of a public business entity.
d. All companies under common control have third-party debt, and each respective company has pledged its assets as collateral for that debt. The

third-party debt on each respective company is personally guaranteed by the owner.

e. Engine Co. assumptions:
   1. Engine Co. was created by the owner to vertically integrate the supply chain for Car Co.'s production of vehicles.
   2. Engine Co. produces engines based on Car Co.'s design specifications.
   3. Engine Co. is the sole engine supplier for Car Co., and substantially all of Engine Co.'s production is sold to Car Co.
   4. No other engines on the market could replace the engines supplied by Engine Co.
   5. During 20XX, Car Co. charged Engine Co. $225,684 for management and other services rendered.
   6. During 20XX, Car Co. purchased $9,482,513 in engines from Engine Co.
   7. Engine Co. has an outstanding loan for $600,000 due to Car Co. that is unsecured and accrues interest at 6 percent. This loan is subordinated to all other debt, and there are no specific repayment terms.
   8. Historically, Car Co. has provided funding to Engine Co. at the request of the owner even though there is no existing contractual requirement to do so.
   9. Total book value of Engine Co.'s liabilities is $2,459,127 as of December 31, 20XX.

f. Tire Co. assumptions:
   1. Tire Co. was created by the owner to vertically integrate the supply chain for the Car Co.'s production of vehicles.
   2. Tire Co. sells a majority of its tires to Car Co.
   3. Many substitutes on the market could replace the tires provided by Tire Co.
   4. During 20XX, Car Co. charged Tire Co. $74,568 for management and other services rendered.
   5. During 20XX, Car Co. purchased $3,792,929 of tires from Tire Co.
   6. Tire Co. has an outstanding loan for $200,000 due to Car Co. that is unsecured and accrues interest at 6 percent. This loan is subordinated to all other debt, and there are no specific repayment terms.
   7. Other than the $200,000 loan, Car Co. has never provided any other additional funding to Tire Co. and is not contractually obligated to do so.
   8. Total book value of Tire Co.'s liabilities is $1,250,000 as of December 31, 20XX.

g. Purse Co. assumptions:
   1. Purse Co. sells high-end designer purses.

2. No significant transactions or arrangements exist between Purse Co. and the other entities under common control.
3. Car Co. did not provide any management services to Purse Co.
4. Car Co. has never provided any additional funding to Purse Co. and is not contractually obligated to do so.
5. Total book value of Purse Co.'s liabilities is $1,000,000 as of December 31, 20XX.

810-10-55-205BE Car Co. meets all the criteria in paragraph 810-10-15-17AD for Engine Co. and Tire Co. and can elect the accounting alternative. As a result of its elected accounting policy, Car Co. would apply the accounting alternative to Engine Co. and Tire Co. on the basis of the following:

a. Car Co. (a private company), Engine Co., and Tire Co. are under common control.
b. Car Co., Engine Co., and Tire Co. are under common control of an individual that is not a public business entity.
c. Neither Engine Co. nor Tire Co. is a public business entity.
d. Car Co. does not directly or indirectly hold a controlling financial interest in Engine Co. or Tire Co. when considering only the General Subsections of this Topic.

Although Purse Co. would not qualify for the accounting alternative because it is a public business entity, Car Co. does not consider Purse Co. to be a legal entity that needs to be assessed for consolidation because Car Co. has no variable interest in Purse Co. Therefore, Car Co. would not provide any disclosures related to Purse Co. under this accounting alternative.

810-10-55-205BF Based on the fact pattern described in paragraphs 810-10-55-205BD through 55-205BE, the following disclosures may satisfy the provisions in paragraphs 810-10-50-2AG through 50-2AI:

a. Engine Company, Inc. (Engine Co.): Engine Co. and Car Company, Inc. (the Company) are under common control. Engine Co. was created by the owner to vertically integrate the supply chain for the Company's production of vehicles. The Company's ability to generate profits depends largely on Engine Co. Engine Co. produces engines for the Company's vehicles in accordance with the Company's design specifications for those engines. Substantially all of Engine Co.'s production is sold to the Company, and Engine Co. is the sole supplier of engines to the Company. No other engines on the market could replace the engines supplied by Engine Co. The Company provides Engine Co. with management and other services (including, but not limited to, accounting, billing, and administrative duties) for which it charged a management fee of $225,684 in 20XX. The Company purchased $9,482,513 of engines during 20XX from Engine Co. Engine Co. has an outstanding loan in the amount of $600,000 due to the Company that is unsecured and accrues interest at

6 percent. The loan is subordinated to all other debt, and no specific repayment terms exist.

b. Tire Company, Inc. (Tire Co.): Tire Co. and the Company are under common control. Tire Co. was created by the owner to vertically integrate the supply chain for the Company's production of vehicles. Tire Co. produces tires for the Company's vehicles and sells a majority of those tires to the Company. The Company provides no design specifications for the tires, and many substitutes on the market could replace the tires that Tire Co. provides. The Company provides Tire Co. with management and other services (including, but not limited to, accounting, billing, and administrative duties) for which it charged a management fee of $74,568 in 20XX. Car Co. purchased $3,792,929 of tires during 20XX from Tire Co. Tire Co. has an outstanding loan in the amount of $200,000 due to the Company that is unsecured and accrues interest at 6 percent. The loan is subordinated to all other debt, and no specific repayment terms exist.

c. Both Engine Co. and Tire Co. have third-party debt, and both companies have their assets pledged as collateral for that debt. The owner of the Company, Engine Co., and Tire Co. has personally guaranteed the third-party debt of the Company, Engine Co., and Tire Co.

d. In addition to the $600,000 loan, the Company historically has been required to provide funds to Engine Co. at the request of the common owner. The Company believes that its maximum financial exposure to loss related to Engine Co. could equal all of Engine Co.'s liabilities. The book value of Engine Co.'s liabilities is $2,459,127 as of December 31, 20XX.

e. Other than the $200,000 loan, the Company has never provided any other additional funding to Tire Co. and is not contractually obligated to do so. The Company believes that its maximum financial exposure related to Tire Co. is limited to the $200,000 loan outstanding and any accrued interest as of December 31, 20XX.

Issue 2: Decision-Making Fees

10. The following are amendments to the evaluation of indirect interests held through related parties under common control when determining whether a decision-making or service provider fee is a variable interest.

Amendments to Subtopic 810-10

11. Amend paragraph 810-10-55-37D, with a link to transition paragraph 810-10-65-9, as follows:

Consolidation—Overall

Implementation Guidance and Illustrations

Variable Interest Entities

> > > Fees Paid to Decision Makers or Service Providers

810-10-55-37D For purposes of evaluating the conditions in paragraph 810-10-55-37, any variable interest in an entity that is held by a **related party** of the decision maker or service provider should be considered in the analysis. Specifically, a decision maker or service provider should include its direct ~~economic~~ variable interests in the entity and its indirect ~~economic~~ variable interests in the entity held through related parties, considered on a proportionate basis. For example, if a decision maker or service provider owns a 20 percent interest in a related party and that related party owns a 40 percent interest in the entity being evaluated, the decision maker's or service provider's interest would be considered equivalent to an 8 percent direct interest in the entity for the purposes of evaluating whether the fees paid to the decision maker(s) or the service provider(s) are not variable interests (assuming that they have no other relationships with the entity). ~~Indirect interests held through related parties that are under common control with the decision maker should be considered the equivalent of direct interests in their entirety.~~ The term *related parties* in this paragraph refers to all parties as defined in paragraph 810-10-25-43, with the following exceptions:

a. An employee of the decision maker or service provider (and its other related parties), except if the employee is used in an effort to circumvent the provisions of the Variable Interest Entities Subsections of this Subtopic.
b. An employee benefit plan of the decision maker or service provider (and its other related parties), except if the employee benefit plan is used in an effort to circumvent the provisions of the Variable Interest Entities Subsections of this Subtopic.

For purposes of evaluating the conditions in paragraph 810-10-55-37, the quantitative approach described in the definitions of the terms *expected losses*, *expected residual returns*, and *expected variability* is not required and should not be the sole determinant as to whether a reporting entity meets such conditions.

12. Add paragraph 810-10-65-9 and its related heading as follows:

Transition and Open Effective Date Information

> Transition Related to Accounting Standards Update No. 2018-17, *Consolidation (Topic 810): Targeted Improvements to Related Party Guidance for Variable Interest Entities*

810-10-65-9 The following represents the transition and effective date information related to Accounting Standards Update No. 2018-17, *Consolidation (Topic 810): Targeted Improvements to Related Party Guidance for Variable Interest Entities*:

a. All entities other than **private companies** shall apply the pending content that links to this paragraph for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years.
b. A private company shall apply the pending content that links to this paragraph for fiscal years beginning after December 15, 2020, and interim periods within fiscal years beginning after December 15, 2021.
c. The pending content that links to this paragraph shall be applied retrospectively with a cumulative-effect adjustment to retained earnings at the beginning of the earliest period presented.
d. Earlier adoption is permitted, including adoption in an interim period.
e. If a reporting entity is required to consolidate a **legal entity** as a result of the initial application of the pending content that links to this paragraph, the initial measurement of the assets, liabilities, and noncontrolling interests of the legal entity depends on whether determining their carrying amounts is practicable. In this context, carrying amounts refer to the amounts at which the assets, liabilities, and noncontrolling interests would have been carried in the consolidated financial statements if the requirements of the pending content that links to this paragraph had been effective when the reporting entity first met the conditions to consolidate the legal entity.
    1. If determining the carrying amounts is practicable, the reporting entity shall initially measure the assets, liabilities, and noncontrolling interests of the legal entity at their carrying amounts at the date the pending content that links to this paragraph first applies.
    2. If determining the carrying amounts is not practicable, the assets, liabilities, and noncontrolling interests of the legal entity shall be measured at **fair value** at the date the pending content that links to this paragraph first applies.
f. Any difference between the net amount added to the statement of financial position of the reporting entity and the amount of any previously recognized interest in the newly consolidated legal entity shall be recognized as a cumulative-effect adjustment to retained earnings at the beginning of the earliest period presented.
g. A reporting entity that is required to consolidate a legal entity as a result of the initial application of the pending content that links to this paragraph may elect the fair value option provided by the Fair Value Option Subsections of Subtopic 825-10 on financial instruments, but only if the reporting entity elects the option for all financial assets and financial liabilities of that legal entity that are eligible for this option under those Fair Value Option Subsections. This election shall be made on a legal entity-by-legal entity basis. Along with the disclosures required in those

Fair Value Option Subsections, the reporting entity shall disclose all of the following:

1. Management's reasons for electing the fair value option for a particular legal entity or group of legal entities
2. The reasons for different elections if the fair value option is elected for some legal entities and not others
3. Quantitative information by line item in the statement of financial position indicating the related effect on the cumulative-effect adjustment to retained earnings of electing the fair value option for a legal entity.

h. If a reporting entity is required to deconsolidate a legal entity as a result of the initial application of the pending content that links to this paragraph, the initial measurement of any retained interest in the deconsolidated former subsidiary depends on whether the determination of its carrying amount is practicable. In this context, carrying amount refers to the amount at which any retained interest would have been carried in the reporting entity's financial statements if the pending content that links to this paragraph had been effective when the reporting entity became involved with the legal entity or no longer met the conditions to consolidate the legal entity.
   1. If determining the carrying amount is practicable, the reporting entity shall initially measure any retained interest in the deconsolidated former subsidiary at its carrying amount at the date the pending content that links to this paragraph first applies.
   2. If determining the carrying amount is not practicable, any retained interest in the deconsolidated former subsidiary shall be measured at fair value at the date the pending content that links to this paragraph first applies.

i. The determinations of whether a legal entity is a **variable interest entity (**VIE) and which reporting entity, if any, should consolidate the legal entity (that is, whether the reporting entity is the **primary beneficiary** of the VIE) shall be made as of the date the reporting entity became involved with the legal entity or, if events have occurred requiring reconsideration of whether the legal entity is a VIE and which reporting entity, if any, should consolidate the legal entity, as of the most recent date at which the pending content that links to this paragraph would have required consideration.

j. If, at transition, it is not practicable for a reporting entity to obtain the information necessary to make the determinations in (i) as of the date the reporting entity became involved with a legal entity or at the most recent reconsideration date, the reporting entity shall make the determinations as of the date on which the pending content that links to this paragraph is first applied.

k. If the determinations of whether a legal entity is a VIE and whether a reporting entity is the primary beneficiary of a VIE are made in accordance with (j), then the consolidating entity shall measure the assets, liabilities, and noncontrolling interests of the legal entity at fair value as of the date on which the pending content that links to this paragraph is first applied. However, if the VIE's activities are primarily related to securitizations or other forms of asset-backed financings and the VIE's assets can be used only to settle the VIE's obligations, then the VIE's assets and liabilities may be measured at their unpaid principal balances (as an alternative to a fair value measurement) at the date the pending content that links to this paragraph is first applied. This measurement alternative does not obviate the need for the primary beneficiary to recognize any accrued interest, an allowance for credit losses, or other-than-temporary impairment, as appropriate. Other assets, liabilities, or noncontrolling interests, if any, that do not have an unpaid principal balance, and any items that are required to be carried at fair value under other applicable Topics, shall be measured at fair value.

l. An entity shall provide the disclosures in paragraphs 250-10-50-1 through 50-2 (excluding the disclosure in paragraph 250-10-50-1(b)(2)) in the period in which the entity adopts the pending content that links to this paragraph.

Amendments to Status Sections

13 Amend paragraph 810-10-00-1 by adding the following items to the table, as follows:

810-10-00-1 The following table identifies the changes made to this Subtopic.

Paragraph	Action	Accounting Standards Update	Date
810-10-15-17AA through 15-17C	Superseded	2018-17	10/31/2018
810-10-15-17AC through 15-17AF	Added	2018-17	10/31/2018
810-10-50-2AD through 50-2AF	Superseded	2018-17	10/31/2018
810-10-50-2AG through 50-2AI	Added	2018-17	10/31/2018
810-10-55-9	Superseded	2018-17	10/31/2018
810-10-55-37D	Amended	2018-17	10/31/2018
810-10-55-205AJ through 55-205AR	Superseded	2018-17	10/31/2018

Paragraph	Action	Accounting Standards Update	Date
810-10-55-205AU through 55-205BF	Added	2018-17	10/31/2018
810-10-65-9	Added	2018-17	10/31/2018

The amendments in this Update were adopted by the vote of five members of the Financial Accounting Standards Board. Mr. Buesser abstained.

Russell G. Golden, *Chairman*
James L. Kroeker, *Vice Chairman*
Christine A. Botosan
Gary R. Buesser
Marsha L. Hunt
R. Harold Schroeder

Background Information and Basis for Conclusions

Background Information

BC1. The following summarizes the Board's considerations in reaching the conclusions in this Update. It includes reasons for accepting certain approaches and rejecting others. Individual Board members gave greater weight to some factors than to others.

BC2. In February 2015, the Board issued Accounting Standards Update No. 2015-02, *Consolidation (Topic 810): Amendments to the Consolidation Analysis.* The amendments in that Update significantly changed the consolidation guidance in Topic 810, particularly in complex areas such as the overall variable interest entity guidance and the analysis of limited partnerships and other similar entities. After the issuance of Update 2015-02, stakeholders expressed concern about the guidance for common control arrangements, including frequent requests from private company stakeholders to clarify how the consolidation analyses for common control arrangements should be performed.

BC3. In June 2016, the Board issued a proposed Update on interests held through related parties under common control. Specifically, the Board proposed a targeted amendment to remove the last sentence of paragraph 810-10-25-42. That sentence required single decision makers to consider indirect interests held through related parties under common control to be the equivalent of direct interests in their entirety as opposed to proportionally. Consequently, when determining whether a single decision maker is the primary beneficiary of a VIE, the single decision maker would include those interests on a proportionate basis to alleviate the concern that a single decision maker with little to no direct and indirect variable interests, nonetheless, could be considered the VIE's primary beneficiary.

BC4. The Board received 18 comment letters on that proposed Update. All respondents supported the Board's proposal to address how a single decision maker would treat indirect interests held through related parties under common control when determining the primary beneficiary of a VIE. However, some stakeholders requested that the Board clarify other aspects of the consolidation guidance for common control arrangements. In October 2016, the Board issued Accounting Standards Update No. 2016-17, *Consolidation (Topic 810): Interests Held through Related Parties That Are under Common Control*. The amendments in Update 2016-17 eliminated the last sentence of paragraph 810-10-25-42; thus, indirect interests held by a single decision maker through related parties under common control are now considered on a proportionate basis instead of as a direct interest.

BC5. In its basis for conclusions of Update 2016-17, the Board acknowledged stakeholders' requests that the Board clarify other aspects of the consolidation guidance for common control arrangements. For example, some stakeholders requested that the Board clarify the guidance in paragraph 810-10-25-44 on determining which party within a related party group is most closely associated with a VIE, noting that the guidance in that paragraph can be difficult to apply. Other stakeholders requested that the Board clarify how to evaluate indirect interests held through related parties that are under common control in paragraph 810-10-55-37D when determining whether a decision maker's fee arrangement represents a variable interest. Those stakeholders stressed the potential link between determining whether a decision maker's fee represents a variable interest and determining which party is the primary beneficiary of a VIE. They emphasized that addressing the fee guidance and primary beneficiary guidance together rather than in a separate initiative may be more efficient and could reduce cost and complexity for preparers, auditors, and users of financial statements.

BC6. The Board decided to research other aspects of the consolidation guidance for common control arrangements as part of a separate initiative, including consideration of issues raised by the Private Company Council (PCC), about private company common control arrangements.

BC7. At a public roundtable meeting held on December 16, 2016, the Board obtained feedback on the following:

a. Whether private companies should be provided with an accounting alternative for common control arrangements, whereby a private company would not have to apply the VIE guidance within Topic 810. Private companies would provide detailed disclosures based on existing related party disclosures in Topic 850, Related Party Disclosures, and existing VIE disclosures (private company accounting alternative).
b. Aligning the consideration of indirect interests held through related parties under common control for determining whether a decision-making or service fee is a variable interest with the determination of whether a single decision maker is the primary beneficiary of a VIE (decision-making fees).
c. Amending the related party guidance for determining whether any party is the primary beneficiary of a VIE if power is shared among related parties or when a related party group under common control has a controlling financial interest in a VIE (VIE related party guidance).

BC8. On the basis of the feedback received at the roundtable meeting and additional outreach performed, the Board issued proposed Accounting Standards Update, *Consolidation (Topic 810): Targeted Improvements to Related Party Guidance for Variable Interest Entities,* on June 22, 2017. The proposed Update addressed the following three issues:

a. Issue 1—Private company accounting alternative
b. Issue 2—Decision-making fees
c. Issue 3—VIE related party guidance.

BC9. The comment period on the proposed Update ended on September 5, 2017, and the Board received 24 comment letters. Respondents broadly supported the amendments in the proposed Update for the private company accounting alternative and decision-making fees. Feedback on whether VIE related party guidance should be amended was mixed. Even those respondents who supported amending that guidance found the amendments as proposed to be inoperable.

BC10. As a result of the feedback received on the proposed Update, the Board affirmed the amendments that address Issues 1 and 2 and decided to remove Issue 3 from its technical agenda at its May 16, 2018 meeting. Those issues are discussed in greater detail in separate sections below.

Benefits and Costs

BC11. The objective of financial reporting is to provide information that is useful to present and potential investors, creditors, donors, and other capital market participants in making rational investment, credit, and similar resource allocation decisions. However, the benefits of providing information for that purpose should justify the related costs. Present and potential investors, creditors, donors, and other users of financial information benefit from improvements in financial reporting, while the costs to implement new guidance are borne primarily by present investors. The Board's assessment of the costs and benefits of issuing new guidance is unavoidably more qualitative than quantitative because there is no method to objectively measure the costs to implement new guidance or to quantify the value of improved information in financial statements. Overall, the Board concluded that the expected benefits of the amendments in this Update justify the expected costs. Detailed discussion on benefits and costs is provided by area in the basis for conclusions below.

Basis for Conclusions

Issue 1—Private Company Accounting Alternative

BC12. The Private Company Decision-Making Framework provides considerations for the Board and the PCC in making user-relevance and cost-benefit evaluations for private companies under the existing conceptual framework. The Private Company Decision-Making Framework is an FASB tool to help the Board and the PCC identify differences in the informational needs of users of public company financial statements and users of private company financial statements and identify opportunities to reduce the relatively greater cost and complexity of preparing financial statements for private companies in accordance with GAAP.

BC13. The Private Company Decision-Making Framework observes that many private companies have multiple entities under common control, which often results in transactions with affiliates and other related parties. In addition, the

Board acknowledged feedback from PCC members who asserted that the VIE guidance within Topic 810 is complex and difficult to apply for private companies under common control. The Board's outreach confirmed the PCC's assertions and helped the Board understand that significant diversity exists in applying consolidation guidance to common control arrangements. The Board learned that inconsistent application of the VIE guidance is most common among practitioners who primarily serve private companies.

BC14. To address the diversity in practice, the Board first attempted to identify potential amendments that would improve the consistency of applying the VIE guidance. However, the Board was unable to identify an approach that was operable. Outreach on this project highlighted that private companies under common control often have no explicit or arm's-length contractual arrangements in place unless required by a third party, which complicates assessing power under the VIE model. The lack of contractual arrangements is the main basis for the Board's conclusion that under the private company accounting alternative, VIE guidance should not be applied to common control arrangements in certain circumstances.

BC15. The Board considered outreach in establishing the scope of the accounting alternative. That outreach found that decision-making rights and power are generally more formalized in a public company setting. Because the Board expects arrangements involving subsidiaries of public business entities to be more formalized, the Board decided against permitting a common control parent to be a public business entity under the accounting alternative. Likewise, the Board decided against permitting a legal entity to be a public business entity under the accounting alternative.

BC16. The Board concluded that an inconsistent consolidation policy within the same reporting entity diminishes user relevance. Thus, the accounting alternative, when elected, must be applied by a private company to all current and future legal entities under common control that meet the criteria for applying the alternative. In other words, the alternative cannot be applied selectively to different common control arrangements.

BC17. Although most stakeholders agree that the private company accounting alternative should apply only to common control arrangements, several stakeholders voiced concerns that common control is not defined in the

Codification. Many private companies currently look to the SEC's observations[1] documented in EITF Issue No. 02-5, "Definition of 'Common Control' in Relation to FASB Statement No. 141," to determine common control, but the Task Force never reached a final consensus on this Issue.

BC18. In the deliberations leading up to Update 2014-07, the Board and the PCC acknowledged stakeholders' concerns but decided against defining *common control*. The Board and the PCC noted that common control exists in other areas of GAAP (for example, to determine the measurement basis for assets purchased under Topic 805, Business Combinations). The Board and the PCC were concerned that such a change could affect all entities, including public business entities. Therefore, the Board and the PCC concluded that the definition of *common control* was outside the scope of Update 2014-07. Furthermore, establishing a definition of *common control* would have required additional analysis, which could have significantly delayed the issuance of Update 2014-07.

BC19. Consistent with its decision in Update 2014-07, the Board did not define *common control* in this Update. However, for the purposes of applying the private company alternative in this Update, the Board continues to believe that the term *common control* should be broader than what the SEC observed in Issue 02-5. For example, an entity owned by a grandparent and an entity owned by a grandchild could, on the basis of facts and circumstances, be considered entities under common control for the purposes of applying the private company accounting alternative.

BC20. In issuing this Update, the Board does not intend to change how practice determines whether an arrangement is under common control for other areas of GAAP. In other words, the Board expects that arrangements that are currently considered to be under common control will continue to be under common control in other areas of GAAP.

BC21. Solely for purposes of applying the private company accounting alternative, the Board concluded that only the voting interest model should be used in determining whether a private company and a legal entity are under common

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[1] . . . the SEC staff has indicated that common control exists between (or among) separate entities only in the following situations:

a. An individual or enterprise holds more than 50 percent of the voting ownership interest of each entity.

b. Immediate family members hold more than 50 percent of the voting ownership interest of each entity (with no evidence that those family members will vote their shares in any way other than in concert).
   (1) Immediate family members include a married couple and their children, but not the married couple's grandchildren.
   (2) Entities might be owned in varying combinations among living siblings and their children. Those situations would require careful consideration regarding the substance of the ownership and voting relationships.

c. A group of shareholders holds more than 50 percent of the voting ownership interest of each entity, and contemporaneous written evidence of an agreement to vote a majority of the entities' shares in concert exists. [paragraph 3 of Issue 02-5] control. Under the voting interest model, the usual condition for a controlling financial interest is ownership of a majority voting interest. Therefore, for purposes of applying this alternative, the Board concluded that only the General Subsections of Topic 810 (and not the VIE Subsections) should be used to determine whether the private company and the legal entity are under common control. The Board reasoned that it would be counterproductive to require the application of the VIE guidance to determine whether a private company is eligible to not apply the VIE guidance.

BC22. The consideration of *indirect* voting ownership is required when determining whether a legal entity qualifies under the accounting alternative. The Board did not intend for the reference to *indirect* to imply that voting interests are to be considered on a proportionate basis. For example, assume Entity A owns 60 percent of the voting interest in Entity B, and Entity B owns 60 percent of the voting interest in Entity C. Because Entity A has a *direct* controlling financial interest in Entity B through its majority ownership and Entity B has a *direct* controlling financial interest in Entity C through its majority ownership, Entity A has an *indirect* interest in Entity C that provides it with a controlling financial interest in Entity C.

BC23. The required disclosures under the accounting alternative are derived from the existing VIE disclosures for a reporting entity that has a variable interest in a VIE but is not the primary beneficiary. The disclosures under the accounting alternative apply only if the legal entity under common control is not consolidated by the private company reporting entity. The Board concluded, and users of private company financial statements stated, that those disclosures provide an understanding of a private company's involvement with and exposure to a legal entity under common control. Users of private company financial statements also stated that the accounting alternative should promote consistency across private companies because it is expected that many private company reporting entities will elect the alternative. Moreover, the Board acknowledged that a reporting entity has the option to combine entities under common control (see paragraph 810-10-55-1B), particularly in situations in which users wish to see the combined results of the reporting entity and another legal entity under common control.

BC24. Effectively, the amendments in this Update expand the alternative for private company leasing arrangements under common control in the VIE guidance provided in the amendments of Update 2014-07. On the basis of outreach with private company stakeholders, the Board concluded that the accounting alternative will continue to address the concerns of private companies currently applying the accounting alternative for leasing arrangements under common control.

BC25. Overall, the private company accounting alternative to allow private companies to forgo applying VIE guidance on common control arrangements meets the Private Company Decision-Making Framework's objective for addressing private company stakeholders' needs. In other words, the accounting alternative should improve decision-useful information for the users of private company financial statements while reducing the cost and complexity associated with applying VIE guidance to private companies under common control.

Issue 2—Decision-Making Fees

BC26. The requirements in paragraph 810-10-55-37 result in a customary, at-market fee not being a variable interest if a decision maker or service provider holds no other interests in the VIE that results in the decision maker absorbing more than an insignificant amount of a VIE's expected losses or receiving more than an insignificant amount of the VIE's expected residual returns. In analyzing whether the decision maker's other interest exposes it to absorbing more than an insignificant amount of a VIE's expected losses or receiving more than an insignificant amount of the VIE's expected residual returns, the decision maker must consider indirect interests held through related parties in addition to its own direct interests.

BC27. Determining whether a decision maker's indirect interests should be considered on a proportional or full attribution basis is critical for determining whether a decision maker applies the rest of the consolidation guidance. Before the amendments in this Update, indirect interests held by related parties under common control with decision makers were required to be considered the equivalent of a direct interest in its entirety (as opposed to proportionally). Thus, that requirement resulted in a greater likelihood that more decision-making fees were determined to be variable interests. Those decision makers were then required to assess their variable interests when determining whether they were the VIE's primary beneficiary. In determining whether they were the VIE's primary beneficiary, the decision makers then would have considered indirect interests held through related parties under common control on a proportionate basis following the amendment resulting from Update 2016-17. Many stakeholders commenting on this issue at the roundtable meeting and during subsequent outreach indicated that indirect interests held through related parties under common control should be considered proportionally when determining whether a decision-making fee is a variable interest. They noted that this would be consistent with how indirect interests held through related parties are considered by single decision makers (that is, proportionally) when determining whether a decision maker is the primary beneficiary of a VIE.

BC28. The Board agreed with those stakeholders and decided to eliminate the requirement in paragraph 810-10-55-37D that "indirect interests held through related parties that are under common control with the decision maker should be considered the equivalent of direct interests in their entirety." The Board agreed that those interests should be considered proportionally instead of on a full attribution basis. The Board reasoned that the existing requirements for considering indirect interests held through related parties under common control inappropriately resulted in decision makers that otherwise would not be the primary beneficiary of a VIE being required to perform the analysis for determining whether they are the primary beneficiary of a VIE and potentially being identified as the primary beneficiary. The Board found no compelling reason to have an inconsistency in how those interests are considered when determining whether a single decision maker is the primary beneficiary of a VIE versus when determining whether a decision-making fee is a variable interest. Finally, the Board concluded that proportional consideration of indirect variable interests is consistent with the economics associated with the related party relationship. That is, the decision maker's economic benefit is only on a proportionate basis and not on a direct basis.

BC29. Separately, to be consistent with the amendments in Update 2016-17, the Board replaced references to *economic* interests with *variable* interests without the intent of changing how the term *interest* is interpreted.

BC30. The Board expects that the amendments in this Update related to decision-making fees will reduce both the cost and complexity in applying consolidation guidance and the redundancy in the disclosure requirements between Topic 606 and Topic 810 while still providing users of financial statements with decision-useful information.

Issue 3—VIE Related Party Guidance

BC31. Situations exist in which power is shared among related parties or related parties under common control that, as a group, have a controlling financial interest even though none of the parties individually concludes that it has a controlling financial interest. A party in those related party groups is required to be identified as the party "most closely associated with" the VIE and, thus, the primary beneficiary. This often is referred to as *forced consolidation*. The Board learned that, broadly, applying the related party guidance in Topic 810 to common control arrangements is a source of complexity and diversity in practice. Specifically, some stakeholders focus on stated power, while others focus on economic exposure to the VIE when applying factors to determine which party is most closely associated with the VIE. In other words, certain stakeholders questioned whether in situations in which it is unclear which party (when power is shared among related parties or within a related party group under common control) has both power and exposure to the economic performance, consolidation should nonetheless be required. The Board also was aware of these concerns from feedback received during its deliberations of Updates 2015-02 and 2016-17, at the roundtable meeting, and through subsequent outreach.

BC32. In the proposed Update, the Board exposed the following amendments to the consolidation guidance for situations in which power is shared among related parties or a related party group of commonly controlled entities holds a controlling financial interest but no single entity within the related party group has a controlling financial interest through its direct and indirect interests:

a. Require consolidation by a single related party if substantially all the activities of a VIE either involve or are conducted on behalf of that party
b. For situations, other than those in (a) above, provide factors for a reporting entity to evaluate in determining whether a related party has a

controlling financial interest in a VIE when power is shared or in a common control arrangement.

BC33. All large practitioners asserted that the amendments to the related party guidance in the proposed Update were inoperable. Of those respondents who noted that the proposed guidance was inoperable, there was diverse feedback on why the guidance was inoperable. Some respondents agreed with the objective of not forcing consolidation for related party common control arrangements (but still found the proposed amendments inoperable as drafted). Other respondents did not want the guidance amended, primarily because of concerns of structuring without *forced consolidation*.

BC34. On the basis of additional outreach and concerns about the amendments to the related party guidance in the proposed Update, the Board decided to remove Issue 3 from its technical agenda and focus on resolving Issues 1 and 2.

Effective Date and Transition

BC35. The Board decided that the amendments in this Update should be effective for entities other than private companies for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. The amendments in this Update will be effective for private companies for fiscal years beginning after December 15, 2020, and interim periods within fiscal years beginning after December 15, 2021. These amendments are required to be applied retrospectively with a cumulative-effect adjustment to retained earnings at the beginning of the earliest period presented. The Board also decided that early adoption should be permitted. Finally, the Board provided practicability provisions to consolidate and deconsolidate a legal entity upon initial adoption of this Update that are consistent with previous Updates, such as Update 2015-02 and Update 2016-17.

Amendments to the XBRL Taxonomy

The amendments to the *FASB Accounting Standards Codification*® in this Accounting Standards Update require improvements to the U.S. GAAP Financial Reporting Taxonomy (Taxonomy). Those improvements, which will be incorporated into the proposed 2019 Taxonomy, are available through Taxonomy Improvements provided at www.fasb.org, and finalized as part of the annual release process.