FINANCIAL ACCOUNTING SERIES

FASB ACCOUNTING STANDARDS UPDATE

No. 2020-01
January 2020

Investments—Equity Securities (Topic 321), Investments—Equity Method and Joint Ventures (Topic 323), and Derivatives and Hedging (Topic 815)

Clarifying the Interactions between Topic 321, Topic 323, and Topic 815

a consensus of the FASB Emerging Issues Task Force

An Amendment of the *FASB Accounting Standards Codification*®

Financial Accounting Standards Board

The *FASB Accounting Standards Codification*® is the source of authoritative generally accepted accounting principles (GAAP) recognized by the FASB to be applied by nongovernmental entities. An Accounting Standards Update is not authoritative; rather, it is a document that communicates how the Accounting Standards Codification is being amended. It also provides other information to help a user of GAAP understand how and why GAAP is changing and when the changes will be effective.

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FASB

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Summary

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

In January 2016, the FASB issued Accounting Standards Update No. 2016-01, *Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*, which added Topic 321, Investments—Equity Securities, and made targeted improvements to address certain aspects of accounting for financial instruments. One of those improvements provided an entity with the ability to measure certain equity securities without a readily determinable fair value at cost, minus impairment, if any. Paragraph 321-10-35-2, as amended, states that if an entity identifies observable price changes in orderly transactions for the identical or a similar investment of the same issuer, it should measure the equity security at fair value as of the date that the observable transaction occurred (hereinafter referred to as the measurement alternative).

Stakeholders raised questions about the interactions between the measurement alternative in Topic 321 and the equity method of accounting in Topic 323, Investments—Equity Method and Joint Ventures. Stakeholders noted that diverse views have emerged about the application of the measurement alternative and the equity method of accounting since the adoption of Update 2016-01. Furthermore, those stakeholders noted that they expect the frequency of these circumstances to increase as more entities adopt the amendments in Update 2016-01 and apply the measurement alternative guidance.

Stakeholders also raised questions about the interactions between Topic 321, Topic 323, and Topic 815, Derivatives and Hedging, related to the application of the guidance for certain forward contracts and purchased options to purchase securities that, upon settlement or exercise, would be accounted for under the equity method of accounting. Stakeholders noted that diverse views have emerged about whether those forward contracts and purchased options should be accounted for in accordance with Topic 321, Topic 323, or Topic 815.

Who Is Affected by the Amendments in This Update?

The amendments in this Update affect all entities that apply the guidance in Topics 321, 323, and 815 and (1) elect to apply the measurement alternative or (2) enter into a forward contract or purchase an option to purchase securities that, upon settlement of the forward contract or exercise of the purchased option, would be accounted for under the equity method of accounting.

What Are the Main Provisions?

The amendments in this Update clarify the interaction of the accounting for equity securities under Topic 321 and investments accounted for under the equity method of accounting in Topic 323 and the accounting for certain forward contracts and purchased options accounted for under Topic 815, as described in the table below.

Area for Improvement	Summary of Amendments
Issue 1: Accounting for Certain Equity Securities upon the Application or Discontinuation of the Equity Method of Accounting Stakeholders asked whether an entity should consider observable transactions that require it to either apply or discontinue the equity method of accounting for the purposes of applying the measurement alternative in accordance with Topic 321.	The amendments clarify that an entity should consider observable transactions that require it to either apply or discontinue the equity method of accounting for the purposes of applying the measurement alternative in accordance with Topic 321 immediately before applying or upon discontinuing the equity method.
Issue 2: Scope Considerations for Forward Contracts and Purchased Options on Certain Securities Stakeholders asked whether certain forward contracts and purchased options to purchase securities that, upon settlement of the forward contract or exercise of the purchased option, would be accounted for under the equity method of accounting in accordance with Topic 323 should be accounted for under Topic 321 or under another Topic. These forward contracts and purchased options do not meet the criteria for derivative accounting under Topic 815 and do not represent in-substance common stock within the scope of Topic 323.	The amendments clarify that for the purpose of applying paragraph 815-10-15-141(a) an entity should not consider whether, upon the settlement of the forward contract or exercise of the purchased option, individually or with existing investments, the underlying securities would be accounted for under the equity method in Topic 323 or the fair value option in accordance with the financial instruments guidance in Topic 825. An entity also would evaluate the remaining characteristics in paragraph 815-10-15-141 to determine the accounting for those forward contracts and purchased options.

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

The amendments in this Update clarify certain interactions between the guidance to account for certain equity securities under Topic 321, the guidance to account for investments under the equity method of accounting in Topic 323, and the guidance in Topic 815, which could change how an entity accounts for an equity security under the measurement alternative or a forward contract or purchased option to purchase securities that, upon settlement of the forward contract or exercise of the purchased option, would be accounted for under the equity method of accounting or the fair value option in accordance with Topic 825, Financial Instruments. These amendments improve current GAAP by reducing diversity in practice and increasing comparability of the accounting for these interactions.

When Will the Amendments Be Effective and What Are the Transition Requirements?

For public business entities, the amendments in this Update are effective for fiscal years beginning after December 15, 2020, and interim periods within those fiscal years. For all other entities, the amendments are effective for fiscal years beginning after December 15, 2021, and interim periods within those fiscal years. Early adoption is permitted, including early adoption in an interim period, (1) for public business entities for periods for which financial statements have not yet been issued and (2) for all other entities for periods for which financial statements have not yet been made available for issuance.

The amendments in this Update should be applied prospectively. Under a prospective transition, an entity should apply the amendments at the beginning of the interim period that includes the adoption date.

Amendments to the *FASB Accounting Standards Codification*®

Introduction

1. The Accounting Standards Codification is amended as described in paragraphs 2–10. 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: Accounting for Certain Equity Securities upon the Application or Discontinuation of the Equity Method of Accounting

Amendments to Subtopic 323-10

2. Amend paragraphs 323-10-35-33 and 323-10-35-36, with a link to transition paragraph 825-10-65-6, as follows:

Investments—Equity Method and Joint Ventures—Overall

Subsequent Measurement

> Change in Level of Ownership or Degree of Influence

> > Increase in Level of Ownership or Degree of Influence

323-10-35-33 Paragraph 323-10-15-12 explains that an investment in common stock of an investee that was previously accounted for on other than the equity method may become qualified for use of the equity method by an increase in the level of ownership described in paragraph 323-10-15-3 (that is, acquisition of additional voting stock by the investor, acquisition or retirement of voting stock by the investee, or other transactions). If an investment qualifies for use of the equity method (that is, falls within the scope of this Subtopic), the investor shall add the cost of acquiring the additional interest in the investee (if any) to the current basis of the investor's previously held interest and adopt the equity method of accounting as of the date the investment becomes qualified for equity method accounting. <u>The</u>

current basis of the investor's previously held interest in the investee shall be remeasured in accordance with paragraph 321-10-35-1 or 321-10-35-2, as applicable, immediately before adopting the equity method of accounting. For purposes of applying paragraph 321-10-35-2 to the investor's previously held interest, if the investor identifies observable price changes in orderly transactions for an identical or a similar investment of the same issuer that results in it applying Topic 323, the entity shall remeasure its previously held interest at fair value immediately before applying Topic 323.

> > Decrease in Level of Ownership or Degree of Influence

323-10-35-36 An investment in voting stock of an investee may fall below the level of ownership described in paragraph 323-10-15-3 from sale of a portion of an investment by the investor, sale of additional stock by an investee, or other transactions and the investor may thereby lose the ability to influence policy, as described in that paragraph. An investor shall discontinue accruing its share of the earnings or losses of the investee for an investment that no longer qualifies for the equity method. The earnings or losses that relate to the stock retained by the investor and that were previously accrued shall remain as a part of the carrying amount of the investment. The investment account shall not be adjusted retroactively under the conditions described in this paragraph. Upon the discontinuance of the equity method, an investor shall remeasure the retained investment in accordance with paragraph 321-10-35-1 or 321-10-35-2, as applicable. For purposes of applying paragraph 321-10-35-2 to the investor's retained investment, if the investor identifies observable price changes in orderly transactions for the identical or a similar investment of the same issuer that results in it discontinuing the equity method, the entity shall remeasure its retained investment at fair value immediately after discontinuing the equity method. Topic 321 also addresses the subsequent accounting for investments in equity securities that are not consolidated or accounted for under the equity method.

Amendments to Subtopic 321-10

3. Amend paragraph 321-10-30-1, with a link to transition paragraph 825-10-65-6, as follows:

Investments—Equity Securities—Overall

Initial Measurement

> Equity Securities Previously Accounted for under the Equity Method

> > Equity Method Is No Longer Appropriate

321-10-30-1 If an **equity security** no longer qualifies to be accounted for under the equity method (for example, due to a decrease in the level of ownership), the security's initial basis for which subsequent changes in fair value are measured shall be the previous carrying amount of the investment. Paragraph 323-10-35-36 states that the earnings or losses that relate to the stock retained by the investor and that were previously accrued shall remain as a part of the carrying amount of the investment and that the investment account shall not be adjusted retroactively. Upon discontinuance of the equity method, an entity shall remeasure the equity security in accordance with~~Subsequently, the security shall be accounted for pursuant to~~ paragraph 321-10-35-1 or 321-10-35-2, as applicable. For purposes of applying paragraph 321-10-35-2 to the investor's retained investment, if the investor identifies observable price changes in orderly transactions for the identical or a similar investment of the same issuer that results in it discontinuing the equity method, the entity shall remeasure its retained investment at fair value immediately after it no longer applies the guidance in Topic 323.

Issue 2: Scope Considerations for Forward Contracts and Purchased Options on Certain Securities

Amendments to Subtopic 815-10

4. Add paragraph 815-10-15-141A and amend paragraph 815-10-15-142, with a link to transition paragraph 825-10-65-6, as follows:

Derivatives and Hedging—Overall

Scope and Scope Exceptions

Certain Contracts on Debt and Equity Securities

> Instruments

815-10-15-141 The guidance in the Certain Contracts on Debt and Equity Securities Subsections applies only to those forward contracts and purchased options having all of the following characteristics:

a. The contract is entered into to purchase securities that will be accounted for under either Topic 320 or Topic 321.

b. The contract's terms require physical settlement of the contract by delivery of the securities.
c. The contract is not a **derivative instrument** otherwise subject to this Subtopic.
d. The contract, if a purchased option, has no intrinsic value at acquisition.

<u>**815-10-15-141A** For the purposes of applying paragraph 815-10-15-141(a) for forward contracts and purchased options, an entity shall not consider whether, upon the settlement of the forward contract or the exercise of the purchased option, individually or with existing investments, the underlying securities would be accounted for under either of the following:</u>

<u>a. The equity method in accordance with Topic 323</u>
<u>b. The fair value option in accordance with Topic 825 if those securities otherwise would have been accounted for under Topic 323.</u>

815-10-15-142 The guidance in the Certain Contracts on Debt and Equity Securities Subsections does not apply to contracts involving securities not within the scope of either Topic 320 or ~~Topic 321~~ <u>Topic 321, after considering the guidance in paragraph 815-10-15-141A</u>.

Amendments to Subtopic 321-10

5. Amend paragraphs 321-10-15-6 and 321-10-55-3, with a link to transition paragraph 825-10-65-6, as follows:

Investments—Equity Securities—Overall

Scope and Scope Exceptions

> Instruments

321-10-15-6 Paragraph 815-10-15-141 explains that the guidance in the Certain Contracts on Debt and Equity Securities Subsections applies to those forward contracts and purchased options that are not derivative instruments subject to Topic 815 but that involve the acquisition of securities that will be accounted for under Topic 321. <u>Paragraph 815-10-15-141A provides guidance on applying the guidance in paragraph 815-10-15-141 to forward contracts and purchased options to purchase securities within the scope of Topic 321.</u>

Implementation Guidance and Illustrations

> Implementation Guidance

> > Scope Application to Certain Instruments and Transactions

> > > Call Options and Forward Contracts on Equity Securities

321-10-55-3 An option to buy an equity security that does not meet the definition of a derivative instrument is within the scope of this Topic. An investment in an option on securities should be accounted for under the requirements of Subtopic 815-10 if the option meets the definition of a derivative instrument, including the criteria for net settlement in paragraph 815-10-15-83(c). This Topic applies to those forward contracts and options that are not derivative instruments subject to Subtopic 815-10 but that involve the acquisition of securities that will be accounted for under this Topic. Paragraph 815-10-15-141A provides guidance on applying the guidance in paragraph 815-10-15-141 to forward contracts and purchased options to purchase securities within the scope of Topic 321.

Amendments to Subtopic 825-10

6. Add paragraph 825-10-65-6 and its related heading as follows:

Financial Instruments—Overall

Transition and Open Effective Date Information

> Transition Related to Accounting Standards Update No. 2020-01, *Investments—Equity Securities (Topic 321), Investments—Equity Method and Joint Ventures (Topic 323), and Derivatives and Hedging (Topic 815): Clarifying the Interactions between Topic 321, Topic 323, and Topic 815*

825-10-65-6 The following represents the transition and effective date information related to Accounting Standards Update No. 2020-01, *Investments—Equity Securities (Topic 321), Investments—Equity Method and Joint Ventures (Topic 323), and Derivatives and Hedging (Topic 815): Clarifying the Interactions between Topic 321, Topic 323, and Topic 815*:

a. For **public business entities**, the pending content that links to this paragraph shall be effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2020.
b. For all other entities, the pending content that links to this paragraph shall be effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2021.
c. Early application of the pending content that links to this paragraph is permitted, including early adoption in an interim period for:

1. Public business entities for periods for which financial statements have not yet been issued
2. All other entities for periods for which financial statements have not yet been made available for issuance.

d. An entity shall apply the pending content that links to this paragraph prospectively at the beginning of the interim period that includes the adoption date.

e. An entity that applies the pending content that links to this paragraph shall disclose the following in the interim and annual periods of the year of adoption:
1. The nature of and reason for the change in accounting principle
2. The transition method
3. A qualitative description of the financial statement line items affected by the change.

Amendments to Status Sections

7. Amend paragraph 321-10-00-1, by adding the following items to the table, as follows:

321-10-00-1 The following table identifies the changes made to this Subtopic.

Paragraph	Action	Accounting Standards Update	Date
321-10-15-6	Amended	2020-01	01/16/2020
321-10-30-1	Amended	2020-01	01/16/2020
321-10-55-3	Amended	2020-01	01/16/2020

8. Amend paragraph 323-10-00-1, by adding the following items to the table, as follows:

323-10-00-1 The following table identifies the changes made to this Subtopic.

Paragraph	Action	Accounting Standards Update	Date
323-10-35-33	Amended	2020-01	01/16/2020
323-10-35-36	Amended	2020-01	01/16/2020

9. Amend paragraph 815-10-00-1, by adding the following items to the table, as follows:

815-10-00-1 The following table identifies the changes made to this Subtopic.

Paragraph	Action	Accounting Standards Update	Date
815-10-15-141A	Added	2020-01	01/16/2020
815-10-15-142	Amended	2020-01	01/16/2020

10. Amend paragraph 825-10-00-1, by adding the following item to the table, as follows:

825-10-00-1 The following table identifies the changes made to this Subtopic.

Paragraph	Action	Accounting Standards Update	Date
825-10-65-6	Added	2020-01	01/16/2020

The amendments in this Update were adopted by the unanimous vote of the seven members of the Financial Accounting Standards Board:

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

Background Information and Basis for Conclusions

Introduction

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

Background Information

BC2. The Board issued Update 2016-01 in January 2016. The amendments in that Update retained the current framework for accounting for financial instruments in GAAP but made targeted improvements to address certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. Equity investments that do not result in the consolidation of an investee and are not accounted for under the equity method of accounting are generally accounted for under Topic 321. The scope of Topic 321 includes equity securities, as defined in the Master Glossary of the Codification, and other ownership interests in an entity, including investments in partnerships, unincorporated joint ventures, and limited liability companies.

BC3. Before the adoption of Update 2016-01, certain equity securities that did not have a readily determinable fair value and that were not accounted for under the equity method were measured at cost, less any impairments that were determined to be other than temporary. The amendments in Update 2016-01 require that an entity measure investments within the scope of Topic 321 with a readily determinable fair value at fair value, with changes in fair value included in net income each reporting period. For investments within the scope of Topic 321 without a readily determinable fair value, an entity may elect to measure those investments at their cost minus impairment (if any). Paragraph 321-10-35-2, as amended, states that if an entity identifies observable price changes in orderly transactions for the identical or a similar investment of the same issuer, it should measure the equity security at fair value as of the date that the observable transaction occurred.

BC4. Topic 323 provides guidance on the equity method of accounting, which applies to investments in common stock or in-substance common stock (or both), including common stock of corporate joint ventures. The equity method of accounting is applied when an investor has the ability to exercise significant influence over the operating and financial policies of an investee. Topic 323 does not apply to investments accounted for in accordance with Topic 810, Consolidation*.*

BC5. Stakeholders raised several questions about the interactions between the measurement alternative in Topic 321 and the equity method of accounting in Topic 323. Stakeholders noted that the measurement alternative was introduced by Update 2016-01 and that, in certain instances, diversity in its application has emerged in practice when applying and discontinuing the equity method of accounting. Furthermore, stakeholders noted that they expect the frequency of these circumstances to increase as more entities adopt the amendments in Update 2016-01 and apply the measurement alternative.

BC6. Stakeholders also raised questions about the interactions between Topic 321, Topic 323, and Topic 815 related to the application of the guidance for certain forward contracts and purchased options to purchase securities within the scope of Topic 321. Topic 815 provides guidance on the accounting for forward contracts and purchased options that have all of the characteristics in paragraph 815-10-15-141, including the characteristic that the contract is entered into to purchase securities that *will* be accounted for under either Topic 320 or Topic 321. Stakeholders noted that diverse views have emerged about the accounting for forward contracts and purchased options on securities that, upon settlement of the forward contract or exercise of the purchased option, would be accounted for under the equity method. Specifically, those stakeholders questioned whether these forward contracts and purchased options should be accounted for in accordance with Topic 321 or another Topic.

BC7. On May 8, 2019, the Board added a narrow-scope project to the EITF agenda to clarify certain interactions between Topic 321, Topic 323, and Topic 815.

BC8. The Board issued proposed Accounting Standards Update, *Investments—Equity Securities (Topic 321), Investments—Equity Method and Joint Ventures (Topic 323), and Derivatives and Hedging (Topic 815): Clarifying the Interactions between Topic 321, Topic 323, and Topic 815*, on July 30, 2019, with a 30-day comment period that ended on August 29, 2019. The Board received 12 comment letters. Overall, respondents supported the amendments in the proposed Update, noting that the amendments provide clarifications of the interactions between these Topics and will generally reduce operational concerns related to the issues discussed in paragraphs BC5 and BC6.

BC9. The Task Force considered feedback received on the proposed Update at its November 7, 2019 meeting and reached a consensus. The Board subsequently ratified the consensus on November 20, 2019, resulting in the issuance of this Update.

Benefits and Costs

BC10. 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 Task Force'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.

BC11. The Task Force does not anticipate that entities will incur significant costs as a result of the amendments in this Update. The Task Force noted that the amendments clarify the interactions between the guidance in Topic 321, Topic 323, and Topic 815 and agreed that the amendments will benefit users by increasing the relevance and comparability of financial statement information. The Task Force also believes that the amendments will result in more consistent application of the guidance and help facilitate financial statement preparers' efforts to implement the amendments in Update 2016-01. The Task Force's specific considerations about costs and benefits of the amendments are further discussed within each of the following sections.

Basis for Conclusions

Issue 1: Accounting for Certain Equity Securities upon the Application or Discontinuation of the Equity Method of Accounting

BC12. An increase in the investment in an investee that was not previously accounted for under the equity method may result in a required change in accounting to the equity method for the investor. For example, an investor acquiring additional voting stock of the investee, the investee acquiring or retiring voting stock, or other capital transactions may result in the investor obtaining significant influence over the investee. Similarly, a decrease in the investment in an investee that was previously accounted for under the equity method may result in the discontinuance of the equity method for the investor. For example, an investor's sale of a portion of an investment in the investee, sale of additional stock by the investee, or other capital transactions may result in the investor losing significant influence over the investee.

BC13. Stakeholders asked whether an observable transaction that results in an investor gaining (or losing) significant influence over the investee and, therefore, results in the investor applying (or discontinuing) the equity method should be considered for purposes of applying the measurement alternative in Topic 321. That is, should an investor remeasure its equity security in accordance with the measurement alternative upon the application or discontinuance of the equity method due to an observable transaction.

BC14. The Task Force reached a consensus that an entity should consider observable transactions that require an investor to apply (or discontinue) the equity method of accounting for the purposes of applying the measurement alternative under Topic 321 immediately before applying (or upon discontinuing) the equity method.

BC15. In reaching its consensus, the Task Force considered the Board's basis for conclusions in Update 2016-01 in which the Board noted that equity securities not accounted for under the equity method of accounting should be measured at fair value through earnings because fair value is a more relevant measurement attribute for equity investments and will be a benefit to financial statement users. On that basis, the Task Force determined that an equity security accounted for in accordance with the measurement alternative should be measured at fair value upon the occurrence of an observable transaction that results in an investor applying or discontinuing the equity method. The Task Force observed that disregarding an observable transaction related to changing measurement methodologies (that is, the application or discontinuation of the equity method) is not consistent with the Board's intent when it issued Update 2016-01. The Task Force also noted that its consensus aligns with the accounting for equity securities with readily determinable fair values, which in practice are remeasured immediately before applying and upon discontinuing the equity method. The Task Force also decided to clarify this accounting in the Codification.

BC16. The Task Force also determined that remeasuring an equity security before applying (or upon discontinuing) the equity method of accounting will provide users with decision-useful information.

Issue 2: Scope Considerations for Forward Contracts and Purchased Options on Certain Securities

BC17. The scope of Topic 321 includes equity securities that, as defined in the Master Glossary and amended by Update 2016-01, include rights to acquire an ownership interest in an entity at a fixed or determinable price (for example, forward purchase contracts and call options). The scope of Topic 321 excludes, among other items, (a) investments accounted for under the equity method in Topic 323 and (b) derivative instruments that are within the scope of Topic 815.

BC18. Topic 321 also notes that certain forward contracts and purchased options that are not derivative instruments subject to Topic 815 but that involve the acquisition of securities that will be accounted for under Topic 321, are accounted for in accordance with the Certain Contracts on Debt and Equity Securities

Subsections of Subtopic 815-10. For those forward contracts and purchased options that are within the scope of Subtopic 815-10 to purchase securities within the scope of Topic 321, the guidance requires that those contracts be measured at fair value in a manner consistent with the guidance in Topic 321.

BC19. The guidance in the Certain Contracts on Debt and Equity Securities Subsections of Subtopic 815-10 applies only to those forward contracts and purchased options that have all of the characteristics in paragraph 815-10-15-141. The characteristic in paragraph 815-10-15-141(a) states that the contract is entered into to purchase securities that will be accounted for under either Topic 320 or Topic 321.

BC20. Stakeholders questioned the interaction of the scope guidance in Topic 321, Topic 323, and Topic 815 for forward contracts and purchased options on securities that, upon settlement or exercise, will be accounted for under the equity method of accounting. Specifically, those stakeholders questioned whether those forward contracts and purchased options would be outside the scope of Subtopic 815-10 because the underlying securities would not be within the scope of Topic 321 upon the settlement of the forward contract or exercise of the purchased option (that is, the contract does not meet characteristic (a) in paragraph 815-10-15-141).

BC21. The Task Force reached a consensus that an entity should not consider whether, upon the settlement of the forward contract or exercise of the purchased option, the underlying securities would individually or with existing investments be accounted for under the equity method for purposes of evaluating characteristic (a) in paragraph 815-10-15-141.

BC22. In response to stakeholder feedback, the Task Force also decided to clarify that an entity should not consider whether, upon the settlement of the forward contract or exercise of the purchased option, the underlying securities would be accounted for under the fair value option in accordance with Topic 825. Stakeholders noted that an entity may elect the fair value option for certain investments that would otherwise be accounted for under the equity method of accounting. Those stakeholders further noted that a similar question could be raised on the accounting for those types of contracts. As a result, the Task Force concluded that an entity should not consider whether, upon settlement of the forward contract or exercise of the purchase option, the underlying securities would be accounted for under the fair value option for purposes of evaluating characteristic (a) in paragraph 815-10-15-141.

BC23. In reaching this consensus, the Task Force considered that entities are required to disregard any potential voting privileges that may become available to holders of securities of an investee when evaluating the requirements to qualify for the equity method in Topic 323. Furthermore, the Task Force concluded that a requirement to consider whether the securities underlying the forward contract or purchased option would be accounted for under the equity method could result in additional complexities in applying the guidance. For example, continuously determining whether an entity would have significant influence over the investee upon settlement of a forward contract or exercise of a purchased option could be complex and operationally burdensome because of changes in the capital structure of the investee.

BC24. Additionally, the Task Force noted that if the forward contracts or purchased options are measured under the equity method of accounting or another cost method, those instruments should be recorded at their initial cost. Generally, at-the-money forward contracts have no cost, or a de minimis cost. For at-the-money purchased options, a premium may be paid to the option writer, but those amounts are generally insignificant compared with the total amount of the purchased securities. As such, the measurement of those forward contracts and purchased options likely will be insignificant, while the economics of those instruments potentially could be significant.

BC25. One Task Force member indicated that the consensus could result in an acquirer being required to measure a forward purchase contract for a controlling financial interest in the acquiree at fair value. That Task Force member noted that practice, in general, has not accounted for these contracts at fair value and that, therefore, the amendments in this Update will change practice for those contracts. However, the Task Force noted that the scope of the amendments clarify, and are limited to, circumstances for which the underlying securities, upon settlement of the forward contract or exercise of the purchased option, individually or with existing investments, should be accounted for under the equity method. The Task Force determined that the amendments will not result in a change in practice for the acquirer’s accounting for forward contracts to purchase a controlling financial interest in an acquiree.

Effective Date and Transition

BC26. The Task Force decided that the amendments in this Update should be effective for public business entities for fiscal years beginning after December 15, 2020, including interim periods within those fiscal years. For all other entities, the Task Force decided to provide a one-year delay, consistent with the Private Company Decision-Making Framework. As such, the amendments in this Update are effective for all other entities for fiscal years beginning after December 15, 2021, including interim periods within those fiscal years. This is consistent with comments from respondents who noted that the amendments would not take a significant amount of time to implement. Early adoption is permitted, including adoption in an interim period.

BC27. The Task Force reached a consensus that requires that an entity apply the amendments in this Update prospectively. In reaching its consensus, the Task Force considered requiring retrospective or modified retrospective application but decided that adjusting the cost basis of an equity method investment for which an entity previously applied the measurement alternative before applying the equity method could be operationally challenging for some financial statement preparers. The Task Force also determined that remeasuring an equity security (including a forward contract or purchased option) to a previous observable transaction would result in a current-period adjustment for a historical fair value measurement that may not be indicative of the current fair value of the equity security and, therefore, may not provide decision-useful information to financial statement users.

BC28. The Task Force reached a consensus not to require any additional recurring disclosures related to equity method investments or equity securities that are accounted for under the measurement alternative because of the limited scope of the amendments in this Update. The Task Force also reached a consensus to require that an entity disclose in the period of adoption the nature of and reasons for the change in accounting principle, the transition method, and a qualitative description of the financial statement line items affected by the change.

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 2020 Taxonomy, are available through Taxonomy Improvements provided at www.fasb.org, and finalized as part of the annual release process.