FASB EXPOSURE DRAFT

Proposed Accounting Standards Update

Issued: December 4, 2014
Comments Due: February 17, 2015

Financial Services—Investment Companies (Topic 946)

Disclosures about Investments in Other Investment Companies

This Exposure Draft of a proposed Accounting Standards Update of Topic 946 is issued by the Board for public comment. Written comments should be addressed to:

Technical Director
File Reference No. 2014-270

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.

Notice to Recipients of This Exposure Draft of a Proposed Accounting Standards Update

The Board invites comments on all matters in this Exposure Draft and is requesting comments by February 17, 2015. Interested parties may submit comments in one of three ways:

- Using the electronic feedback form available on the FASB website at Exposure Documents Open for Comment
- Emailing a written letter to director@fasb.org, File Reference No. 2014-270
- Sending written comments to "Technical Director, File Reference No. 2014-270, FASB, 401 Merritt 7, PO Box 5116, Norwalk, CT 06856-5116."

Do not send responses by fax.

All comments received are part of the FASB's public file. The FASB will make all comments publicly available by posting them to the online public reference room portion of its website.

An electronic copy of this Exposure Draft is available on the FASB's website.

FASB FINANCIAL ACCOUNTING STANDARDS BOARD

Proposed Accounting Standards Update

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December 4, 2014

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Summary and Questions for Respondents

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

During deliberations as part of the investment companies project, the Board discussed concerns about the transparency of information about an investee fund to investors in a reporting investment company. As part of that project, the Board initially decided that an investment company should consolidate investments in other investment companies where it has a controlling financial interest in a fund-of-funds structure. The Board's initial decision was included in the October 2011 proposed FASB Accounting Standards Update, *Financial Services—Investment Companies (Topic 946): Amendments to the Scope, Measurement, and Disclosure Requirements,* which was exposed for public comment.

Stakeholders, however, strongly disagreed with the consolidation requirement in that proposed Update. They stated that transparency could be provided through disclosure about investee funds in the notes to the investment company's financial statements. Furthermore, stakeholders stated that the disclosures would be more decision useful to investors in a reporting investment company if they are required for investments that are significant to the net assets of the reporting investment company and not just those investments that are controlled.

After considering comments on the 2011 proposed Update, the Board decided not to retain the consolidation requirement and, instead, to increase transparency into investee funds by requiring certain disclosures about an investment company's investments in other investment companies. In coming to that conclusion, the Board decided not to require broad disclosures about investments in another investment company. Instead, the Board focused more narrowly on improving existing disclosure requirements in generally accepted accounting principles (GAAP). The guidance in this proposed Update clarifies the scope of disclosure requirements in current GAAP related to investments in other investment companies.

Who Would Be Affected by the Amendments in This Proposed Update?

The amendments in this proposed Update would affect all investment companies within the scope of Topic 946 that have investments in other investment companies. The amendments in this proposed Update would apply to both investment companies regulated under the Investment Company Act of 1940 and those not regulated under that Act.

What Are the Main Provisions?

The amendments in this proposed Update would require a feeder fund in a master-feeder arrangement to provide the master fund's financial statements along with its financial statements. The proposed amendments also would expand the scope of the current requirement to disclose certain information about investments held by investee funds that exceed 5 percent of the reporting entity's net assets to include reporting investment companies that are regulated under the Investment Company Act of 1940.

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

In a master-feeder arrangement, a feeder fund's financial results are driven primarily by the financial results of its master fund. Current Securities and Exchange Commission (SEC) guidance requires a feeder fund that is regulated under the Investment Company Act of 1940 to provide the financial statements of its master fund along with its own financial statements. The amendments in this proposed Update would require similar presentation for all feeder funds not regulated under the Investment Company Act of 1940, resulting in increased consistency and transparency into the master fund in all master-feeder arrangements.

Current GAAP requires an investment company that is not regulated under the Investment Company Act of 1940 to disclose certain information about investments held by investee funds whose fair values exceed 5 percent of the reporting investment company's net assets. The amendments in this proposed Update would require those disclosures to be provided by investment companies that are regulated under the Investment Company Act of 1940, resulting in increased consistency and transparency into investee funds held by all investment companies.

When Would the Amendments Be Effective?

The amendments in this proposed Update would be applied prospectively, and early adoption would be permitted. While this proposed Update does not include a proposed effective date, the Board intends to make the final amendments effective as of the beginning of a reporting investment company's fiscal year and for the interim periods within those fiscal years. The Board will determine the effective date after it considers the feedback on the guidance in this proposed Update.

How Do the Proposed Provisions Compare with International Financial Reporting Standards (IFRS)?

IFRS does not provide comprehensive accounting and reporting guidance for investment companies similar to that in Topic 946. Rather, similar to GAAP, IFRS provides an exception to consolidation guidance for certain controlled investees of an entity that meets the definition of an investment entity. However, due to the differences in the scope of the requirements under IFRS and GAAP, the population of entities that would be affected by the amendments in this proposed Update is broader than the entities that are investment entities under IFRS.

IFRS does not provide specific accounting and reporting guidance for master-feeder arrangements and, therefore, does not require a feeder to attach the master's financial statements along with its financial statements. As part of its investment entity guidance, IFRS requires certain disclosures about investees. However, IFRS does not require specific disclosures about investments held by investee funds of a reporting investment company, as proposed in this Update.

Questions for Respondents

The Board invites individuals and organizations to comment on all matters in this proposed Update, particularly on the issues and questions below. Comments are requested from those who agree with the proposed guidance as well as from those who do not agree. Comments are most helpful if they identify and clearly explain the issue or question to which they relate. Those who disagree with the proposed guidance are asked to describe their suggested alternatives, supported by specific reasoning.

Question 1: Do you agree that all feeder funds in a master-feeder arrangement (those that are regulated under the Investment Company Act of 1940 and those that are not regulated under that Act) should provide the financial statements of their master fund along with their own financial statements? Why or why not?

Question 2: Do you agree that all investment companies (those that are regulated under the Investment Company Act of 1940 and those that are not regulated under that Act) should be required to disclose in their financial statements information about investments held by investee funds that exceed 5 percent of the reporting investment company's net assets? Why or why not?

Question 3: Are the proposed disclosure requirements operable and auditable? If not, which aspects pose operability and/or auditability issues and why?

Question 4: How much time would be necessary to implement the proposed amendments?

Question 5: Should the effective date for investment companies other than public business entities be one year after the first annual period for which public business entities are required to adopt the proposed amendments?

Question 6: Do you agree that the proposed disclosure requirements should be applied prospectively and that early adoption should be permitted? Why or why not?

Amendments to the *FASB Accounting Standards Codification*®

Summary of Proposed Amendments to the Accounting Standards Codification

1. The following table provides a summary of the proposed amendments to the Accounting Standards Codification.

Codification Subtopic	**Description of Changes**
Presentation of Financial Statements (946-205)	• Amended to require a feeder fund to provide the master fund's financial statements along with its own financial statements
Balance Sheet (946-210)	• Clarified the scope of the disclosures about investments held by investee funds to apply to both regulated and nonregulated investment companies

Introduction

2. The Accounting Standards Codification is amended as described in paragraphs 3–5. 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~~.

Amendments to Subtopic 946-205

3. Amend paragraph 946-205-45-6 and its related heading, with a link to transition paragraph 946-210-65-1, as follows:

Financial Services—Investment Companies—Presentation of Financial Statements

Other Presentation Matters

> > ~~Nonpublic~~ Investment Companies Involving Master-Feeder Arrangements

946-205-45-6 ~~Nonpublic investment companies may~~An investment company that is a feeder in a master-feeder arrangement shall present a complete set of ~~master~~the master fund's financial statements with ~~each feeder financial statement, in a manner that is consistent with the requirements for public investment companies.~~its own financial statements.

Amendments to Subtopic 946-210

4. Amend paragraphs 946-210-50-7 through 50-10, with a link to transition paragraph 946-210-65-1, as follows: (Paragraphs 946-210-50-1 and 946-210-50-6 are included for context and represent no change to existing guidance.)

Financial Services—Investment Companies—Balance Sheet

Disclosure

> Schedule of Investments

> > Investment Companies Other than Nonregistered Investment Partnerships

946-210-50-1 In the absence of regulatory requirements, investment companies other than nonregistered investment partnerships shall do all of the following:

a. Disclose the name, share, or principal amount of all of the following:
   1. Each investment (including short sales, written options, futures contracts, forward contracts, and other investment-related liabilities) whose **fair value** constitutes more than 1 percent of net assets. In applying the 1-percent test, total long and total short positions in any one issuer should be considered separately.
   2. All investments in any one issuer whose fair values aggregate more than 1 percent of net assets. In applying the 1-percent test, total long and total short positions in any one issuer should be considered separately.
   3. At a minimum, the 50 largest investments.
b. Categorize investments by both of the following characteristics:
   1. The type of investment (such as common stocks, preferred stocks, convertible securities, fixed income securities, government

securities, options purchased, options written, warrants, futures contracts, loan participations and assignments, short-term securities, repurchase agreements, short sales, forward contracts, other investment companies, and so forth)
    2. The related industry, country, or geographic region of the investment.
c. Disclose the aggregate other investments (each of which is not required to be disclosed by [a]) without specifically identifying the issuers of such investments, and categorize as required by (b). The disclosure shall include both of the following:
    1. The percent of net assets that each such category represents
    2. The total value for category in (b)(1) and (b)(2).

> > Investment Companies that Are Nonregistered Investment Partnerships

946-210-50-6 The financial statements of an investment partnership meeting the condition in paragraph 946-210-50-4 shall, at a minimum, include a condensed schedule of investments in securities owned by the partnership at the close of the most recent period. Such a schedule shall do all of the following:

a. Categorize investments by all of the following:
    1. Type (such as common stocks, preferred stocks, convertible securities, fixed-income securities, government securities, options purchased, options written, warrants, futures, loan participations, short sales, other investment companies, and so forth)
    2. Country or geographic region, except for derivative instruments for which the **underlying** is not a security (see (a)(4))
    3. Industry, except for derivative instruments for which the underlying is not a security (see (a)(4))
    4. For derivative instruments for which the underlying is not a security, by broad category of underlying (for example, grains and feeds, fibers and textiles, foreign currency, or equity indexes) in place of the categories in (a)(2) and (a)(3).
b. Report the percent of net assets that each such category represents and the total value and cost for each category in (a)(1) and (a)(2).
c. Disclose the name, shares or principal amount, value, and type of both of the following:
    1. Each investment (including short sales) constituting more than 5 percent of net assets, except for derivative instruments (see (e) and (f)). In applying the 5-percent test, total long and total short positions in any one issuer should be considered separately.
    2. All investments in any one issuer aggregating more than 5 percent of net assets, except for derivative instruments (see (e) and (f)). In applying the 5-percent test, total long and total short positions in any one issuer shall be considered separately.

d. Aggregate other investments (each of which is 5 percent or less of net assets) without specifically identifying the issuers of such investments, and categorize them in accordance with the guidance in (a). In applying the 5-percent test, total long and total short positions in any one issuer shall be considered separately.
e. Disclose the number of contracts, range of expiration dates, and cumulative appreciation (depreciation) for open futures contracts of a particular underlying (such as wheat, cotton, specified equity index, or U.S. Treasury Bonds), regardless of exchange, delivery location, or delivery date, if cumulative appreciation (depreciation) on the open contracts exceeds 5 percent of net assets. In applying the 5-percent test, total long and total short positions in any one issuer shall be considered separately.
f. Disclose the range of expiration dates and fair value for all other derivative instruments of a particular underlying (such as foreign currency, wheat, specified equity index, or U.S. Treasury Bonds) regardless of counterparty, exchange, or delivery date, if fair value exceeds 5 percent of net assets. In applying the 5-percent test, total long and total short positions in any one issuer shall be considered separately.
g. Provide both of the following additional qualitative descriptions for each investment in another nonregistered investment partnership whose fair value constitutes more than 5 percent of net assets:
    1. The investment objective
    2. Restrictions on redemption (that is, liquidity provisions).

> > Investments in Other Investment Companies

946-210-50-7 This guidance applies to ~~all~~both investment companies regulated under the Investment Company Act of 1940 and investment companies that are not regulated under that Act.

946-210-50-8 Investments in other investment companies (investees), such as investment partnerships, limited liability companies, and funds of funds, shall be considered investments for purposes of applying ~~paragraph~~paragraphs 946-210-50-1~~(a) through (b)~~ and 946-210-50-6.

946-210-50-9 If the reporting investment company's proportional share of any investment owned by any individual investee exceeds 5 percent of the reporting investment company's net assets at the reporting date, each such investment shall be named and categorized as discussed in paragraph 946-210-50-1 or 946-210-50-6, as applicable to the reporting investment company. These investee disclosures shall be ~~made~~ provided either in the ~~condensed~~ schedule of investments (as components of the investment in the investee) or in a note to that schedule.

946-210-50-10 If information about the investments in the investee's portfolio meeting the criterion in paragraph 946-210-50-9 is not available, that fact shall be disclosed.

5. Add paragraph 946-210-65-1 and its related heading as follows:

> Transition Related to Accounting Standards Update No. 2015-XX, *Financial Services—Investment Companies (Topic 946): Disclosures about Investments in Other Investment Companies*

946-210-65-1 The following represents the transition and effective date information related to Accounting Standards Update No. 2015-XX, *Financial Services—Investment Companies (Topic 946): Disclosures about Investments in Other Investment Companies:*

a. The pending content that links to this paragraph shall be effective prospectively for fiscal years, and interim periods within those years, beginning after December 15, 201X.
b. Early adoption of the pending content that links to this paragraph shall be permitted.

The amendments in this proposed Update were approved for publication by the unanimous vote of the seven members of the Financial Accounting Standards Board:

Russell G. Golden, *Chairman*
James L. Kroeker, *Vice Chairman*
Daryl E. Buck
Thomas J. Linsmeier
R. Harold Schroeder
Marc A. Siegel
Lawrence W. Smith

Background Information and Basis for Conclusions

Introduction

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

BC2. The amendments in this proposed Update would require all feeder funds in master-feeder arrangements to provide the master fund's financial statements along with its own financial statements. The proposed amendments also would expand the scope of the current requirement to disclose certain information about investments held by investee funds that exceed 5 percent of the reporting entity's net assets to include reporting investment companies that are regulated under the Investment Company Act of 1940.

Background

BC3. During deliberations, as part of the investment companies project, the Board discussed concerns about the transparency of information about an investee fund to investors in a reporting investment company. In October 2011, the Board issued a proposed Update on the scope, measurement, and disclosure requirements of investment companies. The amendments in that proposed Update would have required an investment company in a fund-of-funds structure to consolidate other investment companies in which it holds a controlling financial interest. At that time, the Board reasoned that consolidation would provide additional transparency about underlying investments and obligations to which the reporting investment company has economic exposure.

BC4. However, in response to the amendments in that proposed Update, stakeholders, including users of investment company financial statements, generally disagreed with consolidation of controlling financial interests in a fund-of-funds structure. Those stakeholders raised conceptual and operability concerns with the requirements. Many stakeholders stated that the transparency about the assets, liabilities, income, and expenses of a controlled investee fund could be addressed more effectively through expanded disclosures in the notes to the investment company's financial statements rather than through consolidation of the controlled investee fund. Those stakeholders stated that information should be provided about investee funds that are significant to the reporting investment company's net assets and not just those that are controlled.

BC5. Consistent with the feedback received on the amendments in the 2011 proposed Update, the Board decided to require certain disclosures about investments in investee funds. However, throughout deliberations, the Board had difficulty developing disclosures that would benefit users and justify the costs. As such, the Board decided not to proceed with broad disclosures about investments in other investment companies. Rather, the Board decided to make improvements to current disclosure requirements in GAAP.

Master-Feeder Arrangements

BC6. The Board understands that the SEC requires feeder funds that are regulated under the Investment Company Act of 1940 to provide the financial statements of the master fund along with their financial statements. The Board received feedback from stakeholders that almost all feeder funds that are not regulated under the Investment Company Act of 1940 also provide master fund financial statements consistent with the requirement for investment companies regulated under that Act. The Board's proposed requirement would improve accounting standards by including this current practice and requiring it for all feeder funds regardless of whether they are regulated under the Investment Company Act of 1940.

BC7. The Board discussed whether a definition of master-feeder arrangements is necessary for investment companies to comply with the proposed disclosure requirement. The Board decided that a definition was not needed because, in current practice, investment companies must already determine whether the structure is a master-feeder arrangement to comply with GAAP. For example, current GAAP requires a feeder fund to report separately the feeder's allocated share of the master fund's investment income and realized and unrealized gains and losses. The Board believes that the proposed requirement to provide a master fund's financial statements along with a feeder fund's financial statements should not result in a change to the determination of whether a structure continues to be a master-feeder arrangement. Furthermore, the Board believes that including a definition of master-feeder arrangements may change practice inappropriately by excluding certain investment company structures, resulting in a loss of information for investors in those arrangements.

Investments Held by Investee Funds

BC8. The guidance in this proposed Update would expand the scope of the current requirement in paragraph 946-210-50-9 to disclose certain information about investments held by investee funds that exceed 5 percent of the reporting entity's net assets by requiring those disclosures to also be provided by investment companies that are regulated by the Investment Company Act of 1940. The Board believes that this disclosure requirement should be the same for all investment companies regardless of whether they are regulated by the Investment Company Act of 1940.

Effective Date and Transition

BC9. The Board decided that the amendments in this proposed Update would be applied prospectively because the costs of a retrospective application would not justify its benefits.

BC10. While this proposed Update does not set a proposed effective date, the Board intends to make the final amendments effective as of the beginning of a reporting investment company's fiscal year and for the interim periods within those fiscal years. The Board will determine the effective date after it considers the feedback on the guidance in this proposed Update. Early adoption would be permitted.

BC11. Regarding the applicability of the proposed amendments to investment companies other than public business entities, the Board has not yet determined whether those entities should have a one-year deferral in the effective date as discussed in the *Private Company Decision-Making Framework: A Guide for Evaluating Financial Accounting and Reporting for Private Companies*. In that context, the Board notes that many investment companies that are not public business entities have adequate resources to comply with GAAP and sophisticated users that can benefit from the additional proposed disclosures. Therefore, the Board questions whether the one-year deferral described in that Guide should apply to the proposed disclosure requirements for investment companies that are other than public business entities. To further deliberate those matters, the Board is requesting feedback specifically in a question to investment companies that are other than public business entities.

Benefits and Costs

BC12. 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. Existing 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.

BC13. The Board recognizes that the requirement to provide the master fund's financial statements only would affect nonregulated funds because it is currently a requirement for funds regulated under the Investment Company Act of 1940. Also, auditors have stated that, in practice, the master fund's financial statements are almost always provided, even for nonregulated funds. Therefore, this requirement would likely not result in additional costs or change in practice for most entities. Regarding the disclosure requirements for investments held by investee funds, the Board believes that the information about the investment portfolio of an investee fund should be available to investment companies without significant costs. However, the practicability exemption has been maintained; as such, if the information about the investee's portfolio is not available, the investment company is only required to disclose that fact. This exemption will reduce costs for those investment companies. The Board believes that both proposals would be supportive of increased comparability through consistent application by all investment companies.

BC14. The Board believes that these benefits would justify the costs of providing the proposed disclosures. The Board decided on the proposed disclosures because they are direct and easily accessible, which should reduce costs. The Board is seeking further input about the proposed disclosures by including a specific question regarding operability and auditability in this proposed Update.

Amendments to the XBRL Taxonomy

Investment companies regulated under the SEC's Investment Company Act of 1940 are currently not required to file an XBRL exhibit with the SEC. As a result, guidance in Topic 946 is not included in the U.S. GAAP Financial Reporting Taxonomy (UGT). Therefore, no change will be made to the UGT as a result of this proposed Update.