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FASB Proposes to Reorganize Its Consolidation Guidance

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On September 20, 2017, the FASB issued for public comment a proposed ASU[1] that would reorganize the consolidation guidance in ASC 810[2] by creating a new Codification topic, ASC 812, with separate sections for the guidance on (1) the variable interest entity (VIE) model and (2) the voting interest entity model. The goal of the proposed ASU is to make "navigating and understanding consolidation guidance easier without affecting how consolidation analyses are currently performed." Comments on the proposed ASU are due by December 4, 2017.

Background

ASC 810 contains multiple consolidation models, including the VIE model, the voting interest entity model, and the model for entities controlled by contracts. The guidance in those models and elsewhere in ASC 810 is often viewed as difficult to navigate because it is not presented in the sequence in which an entity would perform a consolidation analysis.[3] ASC 810 also contains certain terminology that is considered overly complex.

[1] FASB Proposed Accounting Standards Update, *Consolidation (Topic 812), Reorganization*.

[2] FASB Accounting Standards Codification (ASC or the "Codification") Topic 810, *Consolidation*.

[3] For instance, determining whether a legal entity is being evaluated is the first step performed in the consolidation evaluation. See Deloitte's *A Roadmap to Consolidation — Identifying a Controlling Financial Interest* ("Deloitte's Consolidation Roadmap"), including the decision tree on page 8, which illustrates our view of the sequencing of steps to be performed under ASC 810.

Key Provisions of the Proposed ASU

No Expected Changes to Consolidation Outcomes or Conclusions

The FASB does not expect there to be changes to an entity's previous consolidation outcomes or conclusions as a result of the proposed amendments.

Connecting the Dots

If the proposal is finalized, stakeholders will be required to amend their previously documented consolidation conclusions by replacing ASC 810 citations with references to ASC 812, which may be a burdensome task. Unlike the original guidance issued in the Codification, for which the FASB provided a reverse look-up reference tool, references to the original pronouncements in every paragraph, and a quick-reference guide for locating codified guidance, the proposed ASU contains no cross-reference resources.

Consolidation of Entities Controlled by Contract

The FASB received feedback from stakeholders that the guidance on the consolidation of entities controlled by contract applies in only limited circumstances to not-for-profit entities. Accordingly, the proposed ASU would move that guidance to ASC 958.[4]

Terminology, Including the Term "Expected"

In response to feedback from stakeholders that certain terminology is overly complex, the FASB proposes to clarify its use of the term "expected," which appears in several contexts in the VIE guidance in ASC 810, such as in the phrase "expected losses and expected residual returns" of a VIE.[5] The proposed ASU explains that while the determination of such losses and returns involves a quantitative calculation, those amounts "can usually be determined qualitatively." However, the Board does not expect there to be changes to outcomes as a result of the clarified terminology since most preparers and practitioners are already performing qualitative assessments in such circumstances.

The FASB also proposes to amend certain paragraphs in ASC 810 to revise language that contains negative and double-negative references. Examples of such language are contained in ASC 810-10-15-14, which outlines three criteria, one of which must be met for a legal entity to qualify as a VIE. To clarify that language, the FASB would replace ASC 810-10-15-14 with proposed ASC 812-20-25-23.[6]

Connecting the Dots

To highlight what has changed when it amends a standard, the FASB typically underlines additions and strikes out deletions. However, the changes discussed above have not been underlined or stricken in the proposed ASU. Accordingly, we caution stakeholders that the proposed ASU may contain additional changes to language that are not readily apparent.

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[4] FASB Accounting Standards Codification Topic 958, *Not-for-Profit Entities*.

[5] See Appendix C of Deloitte's Consolidation Roadmap for discussion of expected losses and expected residual returns.

[6] ASC 810-10-15-14 states, in part (emphasis added):

> "**A legal entity shall be subject to consolidation under the guidance in the Variable Interest Entities** Subsections if, by design, any of the following conditions exist. . . .
>
> a. The **total equity investment** (equity investments in a legal entity are interests that are required to be reported as equity in that entity's financial statements) **at risk is not sufficient to permit the legal entity to finance** its activities without additional subordinated financial support provided by any parties, including equity holders."

Proposed ASC 812-20-25-23 states, in part (emphasis added):

> "**A legal entity is not a VIE and, thus, is a voting interest entity subject to the guidance in Subtopic 812-30 if, by design, all of the following conditions exist**. . . .
>
> a. **The total equity investment** (equity investments in a legal entity are interests that are required to be reported as equity in that entity's financial statements) **at risk is sufficient to permit the legal entity to finance** its activities without additional subordinated financial support provided by any parties, including equity holders."

Effective Date and Transition

The FASB plans to determine an effective date for the final guidance after considering stakeholder feedback on the proposed ASU.

If an entity has not already adopted ASU 2015-02,[7] it would be required to apply the guidance in the proposed ASU concurrently with the amendments in ASU 2015-02 and use the same transition method. If an entity has already adopted ASU 2015-02, it would be required to apply the proposed ASU's amendments retrospectively to all relevant prior periods beginning with the year it initially applied the amendments in ASU 2015-02.

Connecting the Dots

Although the FASB does not expect consolidation outcomes or conclusions to change as a result of the amendments, the proposed ASU contains transition guidance. On the basis of Board discussions, we understand that the transition guidance would apply to circumstances in which a reporting entity may have reached a different conclusion as a result of its improved understanding of the consolidation guidance under the reorganization and clarifications.

7 FASB Accounting Standards Update No. 2015-02, *Amendments to the Consolidation Analysis*.

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