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Accounting Journal Entry

FASB Issues Final Standard on Simplifying the Equity Method of Accounting

March 16, 2016 — Yesterday, the FASB issued ASU 2016-07,[1] which simplifies the equity method of accounting by eliminating the requirement to retrospectively apply the equity method to an investment that subsequently qualifies for such accounting as a result of an increase in the level of ownership interest or degree of influence. Consequently, when an investment qualifies for the equity method (as a result of an increase in the level of ownership interest or degree of influence), the cost of acquiring the additional interest in the investee would be added to the current basis of the investor's previously held interest, and the equity method would be applied subsequently from the date on which the investor obtains the ability to exercise significant influence over the investee. The ASU further requires unrealized holding gains or losses in accumulated other comprehensive income related to an available-for-sale security that becomes eligible for the equity method to be recognized in earnings as of the date on which the investment qualifies for the equity method.

Effective Date and Transition

The guidance is effective for all entities for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years, with early adoption permitted for all entities. Entities are required to apply the guidance prospectively to increases in the level of ownership interest or degree of influence occurring after the ASU's effective date. Additional transition disclosures are not required upon adoption.

Status of Other Simplification Initiatives Related to the Equity Method of Accounting

The FASB's equity method simplification project initially also included a proposal to eliminate the requirement to account for basis differences.[2] However, after evaluating the feedback received on the proposal, the FASB decided to conduct further research and address the issue separately from the requirement to eliminate the retrospective application of the equity method (which is addressed by ASU 2016-07). The FASB staff is currently conducting such research and has yet to announce the timing for redeliberating and finalizing this issue.

[1] FASB Accounting Standards Update No. 2016-07, *Simplifying the Transition to the Equity Method of Accounting*.

[2] A basis difference can be defined as the amount by which the cost of acquiring an equity method investment exceeds the investor's proportionate interest in the net assets of the investee.