

May 15, 2013

SENT VIA EMAIL

Ms. Susan M. Cospers, Technical Director
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

Re: File Reference: 2013-220 - Proposed Accounting Standards Update, *Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*.

Dear Ms. Cospers,

Moss Adams LLP is pleased to provide a response to the Financial Accounting Standards Board's Proposed Accounting Standards Update, *Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities* (the "proposed ASU").

Moss Adams LLP is the largest accounting and consulting firm headquartered in the Western United States, with a staff of over 2,000, including more than 260 partners. Founded in 1913, the firm serves public and private middle-market businesses, not-for-profit and governmental organizations.

We appreciate the Financial Accounting Standard Board's ("the Board") efforts to comprehensively review the accounting for financial instruments, including its joint deliberations with the International Accounting Standards Board. In an increasingly complex and globally connected world, our firm and the middle-market companies we serve routinely operate internationally, and we believe the joint convergence efforts of the two Boards is both desirable and necessary to improve financial reporting and avoid unnecessary costs in the financial reporting system.

Our response and related comments to the specific questions included within the exposure draft are contained in the Attachment to this letter. In addition to responding to the specific questions asked in the proposed ASU, our general observations on the proposal are as follows:

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Support for the overall direction of the proposed ASU

Overall, we support the Board's efforts to improve the accounting for financial instruments by proposing a model that accounts for the substance of an instrument, rather than its legal form, in the recognition and subsequent measurement of a financial asset. We also support the continued use of three classification categories, including retaining amortized cost and fair value through other comprehensive income categories. We believe that, when coupled with the Board's proposed impairment model (Proposed ASU 2012-260), the financial assets recognized and measured on balance sheets of financial services entities should provide users with more decision-useful information about the entity as compared to the existing accounting standards.

Application and scalability of the proposed guidance to non-financial and smaller entities

In our view, the proposed ASU lacks sufficient implementation and application guidance for both non-financial entities and smaller financial entities, such as manufacturing companies and community banks, respectively. As currently drafted, it is unclear how the business model criterion should be applied for these entities and, specifically, at what level the guidance should be applied. In the context of a hypothetical typical community bank, for example, it is not clear whether the application of the indicators identified in paragraphs 825-10-55-28 and 55-29 should result in the bank having one business model or multiple business models. While granular information about classes of financial assets is provided to key management personnel, which may be an indicator the bank has multiple business models, executive management is typically compensated based upon the overall performance of the entity. Further, a community bank does not typically have a distinctive legal or organizational structure, or management team over financial assets that would indicate there is more than one business model. A weighting of these indicators could be interpreted as the bank having a single business model. In order to prevent diversity in practice in how this guidance is applied, we encourage the Board to include additional guidance on how to apply the business model criterion to smaller financial entities, and we urge the application guidance to permit an appropriately granular view of the business model criterion while acknowledging that many smaller financial entities consider themselves to operate in one line of business and with one business model.

With respect to non-financial entities, we have similar concerns as those expressed in the previous paragraph. Specifically, the application guidance in the proposed ASU does not provide practical guidance in identifying the appropriate level at which to apply the business model criterion. In many non-financial entities, and particularly smaller entities, the management of financial assets is a secondary, tertiary, or lower aspect of managing the business and it may be challenging for these entities to identify multiple business models for its financial assets. We expect that smaller non-financial entities are likely to recognize their financial assets (including accounts receivable) under the measurement model of amortized cost, as the intent would be for the entity to hold the financial

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assets for contractual cash flows. However, we are concerned that smaller non-financial entities that are unable to identify more than one business model and have occasionally sold financial assets in the past will be required to apply the fair value with changes in fair value through other comprehensive income measurement model. The resulting fair value measurement requirements for all of the financial assets would be challenging to apply. Even today, smaller entities continue to struggle with the requirements in Accounting Standards Codification Topic 820, frequently outsourcing the analysis and disclosure work for all fair value measurements as they typically lack the internal resources to appropriately address the inherent complexity of fair value measurements and disclosures.

While we are supportive of the Board's approach to develop principles-based guidance that can be applied across entities, the principles must be scalable to the size and complexity of an organization so users are provided appropriate information at a reasonable cost to preparers. For the principles in the proposed ASU, it is not clear to us that this threshold has been met, and we encourage the Board to either modify the principles or provide more application guidance to clarify how the principles are scalable across entities in different industries and of different sizes. Finally, it is unclear to us if the input of the Private Company Council will be solicited and incorporated into the proposed guidance for nonpublic entities, and we encourage the Board to take this additional step in its deliberations.

Moss Adams appreciates the opportunity to comment on the proposed ASU. We would be pleased to discuss our comments with the Board members or the FASB staff at your convenience. If you would like to discuss our comments or have any questions, please contact John Donohue in our Professional Practice Group at 206-302-6800.

Yours truly,

Moss Adams LLP

ATTACHMENT

The following are responses to selected questions in the exposure draft:

Question 1 - Do you agree with the scope of financial instruments included in this proposed Update? If not, which other financial instruments should be included or excluded from the guidance in this proposed Update and why?

Overall, we agree with the scope of financial instruments included in the proposed Update.

Question 2 - Do you agree with the industry-specific specialized guidance scope exceptions in paragraph 825-10-15-9? If not, why? What would you propose instead?

We agree with the scope exceptions for the industry-specific specialized guidance as detailed in proposed paragraph 825-10-15-9.

Question 4: Do the proposed amendments appropriately convey the principle associated with the contractual cash flow characteristics assessment? If not, why? What would you propose instead?

The basic principle describing the contractual cash flow characteristic in proposed paragraph 825-10-25-17 is appropriately conveyed. However, we believe additional clarification is necessary on how paragraph 825-10-25-20 should be applied, particularly to smaller, less complex entities.

For example, contractually permitted “default rates” of interest are common in loans made by community banks. At inception, a bank would usually consider the default of an individual loan to be remote and included to protect the bank’s position if foreclosure became necessary. It is unclear to us how proposed paragraphs 825-10-55-24 and 55-25 should interact in applying the cash flow characteristic to the default rate example, as 55-24 requires an entity to disregard contingent terms if it is based on “an event that is extremely rare, highly abnormal, and very unlikely to occur,” while 55-25 provides an example of a punitive rate imposed due to the occurrence of a contingent event and states that this instrument would not meet the contractual cash flow characteristic criterion. We do not think it is the Board’s intent to cause wholesale changes to the standard banking terms of community banks in order to meet the cash flow characteristic, and we encourage the Board to perform additional outreach and consider further clarifying the nature of events that would be permitted to pass the contractual cash flow characteristics criterion.

We also believe the Board should revisit its application guidance surrounding the “modified economic relationship” in proposed paragraphs 825-10-55-17 through 55-20. While we understand that the Board has concerns about the potential abuse of having embedded interest rate derivatives or improper use of leverage within contractual interest terms, we fail to see how

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the example described in proposed paragraph 825-10-55-20 is so abusive that the instrument should fail the contractual cash flow characteristic criterion.

Finally, in applying the comparison of an instrument to a hypothetical benchmark instrument described in paragraphs 55-18 and 55-19, we believe that examples of this analysis should be added to the application guidance as the comparison may be challenging for constituents to apply, particularly the assessment of whether a difference is “insignificant.” While we acknowledge that the Board is reluctant to provide bright-line interpretive guidance, we would prefer the Board provide such guidance up front, rather than ex-post interpretations from the international accounting firms or securities regulators.

Question 5: The proposed amendments define principal as the amount transferred by the holder at initial recognition. Should the definition of principal be expanded to include repayment of the principal amount at maturity or other settlement? If so, what instruments would fail (or pass) the contractual cash flow characteristics criterion as a result of this change?

We believe that the definition of principal should be expanded to include repayment of the principal amount at maturity or other settlement. Additionally (or potentially alternatively), we also believe that additional guidance should be provided on the unit of account for instruments with multiple disbursements. For example, for a line of credit with a small initial disbursement and subsequent disbursements at unscheduled points in the future, if only the initial disbursement is considered principle and the entire instrument is considered the unit of account, the instrument would appear to fail the contractual cash flow characteristic criterion. We do not believe it was the Board’s intent to have standard line of credit arrangements fail the criterion, and we encourage the Board to consider the modifications described above, including how these provisions operate “at initial recognition.”

A second area relates to unpaid accrued interest, which is not addressed in the definition of principal, but is described in proposed paragraph 825-10-55-60 as failing the cash flow characteristic assessment when interest is not accrued on unpaid accrued interest. This implies that unpaid accrued interest is viewed by the Board as principal, and we believe the guidance should be revised to reflect this view.

Question 6: Do the proposed amendments contain sufficient application guidance and illustrations on implementing the cash flow characteristics assessment? If not? Why?

We believe the proposed amendments should include more application guidance and illustrations for non-financial and smaller, less complex entities, as a large number of these entities would be required to apply this guidance to relatively straightforward instruments, and these constituents

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would benefit from the additional examples. Also, in some cases, the application guidance and illustrations should provide a more robust analysis for reaching conclusions on all of the relevant points. For example, we observed that proposed paragraph 825-10-55-67 fails to analyze the most challenging point of analysis related to evaluating whether subordinated tranches meet the conditions in proposed paragraph 825-10-55-26(c), which greatly reduces the helpfulness of the example. We recommend that the Board expand the application guidance to provide an example of the subordinated tranche condition demonstrating how the condition would be passed and failed in the context of the original example. A similar approach should be taken to other examples where appropriate.

Question 7: Should a financial asset with a contractual term that modifies the economic relationship (see paragraphs 825-10-55-17 through 55-20) between principal and interest be considered to contain cash flows that are solely payments of principal and interest? Should this be the case if, and only if, the contractual cash flows could or could not be more than insignificantly different from the benchmark cash flows as discussed in paragraph 825-10-55-19? If not, why? What would you propose instead?

Please see our response to Question 4.

Question 8: Do the proposed amendments contain sufficient application guidance in paragraphs 825-10-55-17 through 55-20 on assessing a modified economic relationship? If not, why?

As indicated in response to Question 4, we believe further clarification should be provided.

Question 9: For beneficial interests in securitized financial assets, the proposed amendments would require an entity to look through to the underlying pool of instruments in determining whether the tranche contains payments of solely principal and interest. Do you agree with this look-through approach? If not, why? What would you propose instead?

We understand the Board's conceptual reasons for its approach to evaluating beneficial interests in securitized financial assets, and we generally agree with those reasons. However, we believe the proposed amendments lack operability at a reasonable cost for smaller entities.

Frequently, smaller entities will engage third parties to provide investment management and reporting services, as a smaller entity does not have the resources to hire an individual with the appropriate skill and background to perform these services. The analysis required by 825-10-55-26 will be outsourced to third parties in most of these situations, further increasing the financial

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reporting cost to smaller entities. Other provisions of the guidance, such as the requirement to “look through until the underlying pool of instruments can be identified” will most likely be outsourced or delegated to an investment manager, particularly for more complex instruments such as purchased re-securitization instruments.

For entities unable or unwilling to invest the resources in this analysis, the provision in 825-10-55-27 will require accounting for the instrument at fair value through net income. We agree that this is an appropriate measurement model for instruments where appropriate information cannot be obtained. However, our observation is that smaller entities are most likely to lack the resources to perform a proper analysis and will therefore have additional instruments recognized at fair value through net income as these are the entities that struggle the most with fair value measurement and disclosure. We encourage the Board and/or the Private Company Council to take this into consideration when considering exceptions for smaller and nonpublic entities.

Finally, we observe that it will be costly to audit the information necessary to support the analysis of the underlying instruments, the tranche’s payments, and the relative positions of the tranches of underlying instruments and how that affects the evaluation of credit risk as discussed in paragraph 825-10-55-26 c. Similar to smaller entities, many audit firms will also have to identify independent third-party sources to assist in corroborating management’s assertions, leading to increased audit costs. We ask that the Board carefully weigh these additional costs in its analysis of costs and benefits for the proposed guidance.

Question 10: Do the proposed amendments appropriately convey the principle associated with the business model assessment? If not, why? What would you propose instead?

While the response to this question is included in our cover letter, we have reproduced the comment here for completeness:

In our view, the proposed ASU lacks sufficient implementation and application guidance for both non-financial entities and smaller financial entities, such as manufacturing companies and community banks, respectively. As currently drafted, it is unclear how the business model criterion should be applied for these entities and, specifically, at what level the guidance should be applied. In the context of a hypothetical typical community bank, for example, it is not clear whether the application of the indicators identified in paragraphs 825-10-55-28 and 55-29 should result in the bank having one business model or multiple business models. While granular information about classes of financial assets is provided to key management personnel, which may be an indicator the bank has multiple business models, executive management is typically compensated based upon the overall performance of the entity. Further, a community bank does not typically have a distinctive legal or organizational structure or management team over financial assets that would indicate there is more than one business model. A weighting of these indicators could be interpreted as the bank having a single business model. In order to prevent

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diversity in practice in how this guidance is applied, we encourage the Board to include additional guidance on how to apply the business model criterion to smaller financial entities, and we urge the application guidance to permit an appropriately granular view of the business model criterion while acknowledging that many smaller financial entities consider themselves to operate in one line of business and with one business model.

With respect to non-financial entities, we have similar concerns as those expressed in the previous paragraph. Specifically, the application guidance in the proposed ASU does not provide practical guidance in identifying the appropriate level at which to apply the business model criterion. In many non-financial entities, and particularly smaller entities, the management of financial assets is a secondary, tertiary, or lower aspect of managing the business and it may be challenging for these entities to identify multiple business models for its financial assets. We expect that smaller non-financial entities are likely to recognize their financial assets (including accounts receivable) under the measurement model of amortized cost, as the intent would be for the entity to hold the financial assets for contractual cash flows. However, we are concerned that smaller non-financial entities that are unable to identify more than one business model and have occasionally sold financial assets in the past will be required to apply the fair value with changes in fair value through other comprehensive income measurement model. The resulting fair value measurement requirements for all of the financial assets would be challenging to apply. Even today, smaller entities continue to struggle with the requirements in Accounting Standards Codification Topic 820, frequently outsourcing the analysis and disclosure work for all fair value measurements as they typically lack the internal resources to appropriately address the inherent complexity of fair value measurements and disclosures.

Question 11: Do the proposed amendments provide sufficient application guidance and illustrations on how to distinguish among the three business models, including determining whether the business model is to manage assets both to collect contractual cash flows and to sell? Do you agree with the proposed guidance provided to describe those business models? If not, why?

As noted in our comments in the cover letter and above, we believe additional application guidance and illustrations are necessary, particularly for non-financial entities and smaller financial entities. In addition, we also believe that further clarification should be provided on how entities would determine when a change in business model may have occurred, or when a change in business model occurs over time, that is not a result of a discrete event. For example, for an entity that has a business model that is to manage assets to both collect contractual cash flows and to sell, there may be gradual changes in operations of the environment over time that may cause sales of financial assets to be a greater (or smaller) proportion of the portfolio, such that the initially selected business model is no longer most appropriate. In this instance, application of

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proposed paragraphs 825-10-35-22 would preclude a change in business, resulting in a continuation of the existing business model. If this is not the Board's intent, further guidance, particularly in proposed paragraphs 825-10-55-86 and 55-87 should be provided. This scenario may also be an example of where an allocation between business models is appropriate, as permitted by proposed paragraph 825-10-25-30. We recommend the Board clarify the application of these principles by providing additional application guidance.

Question 12: Should the classification and measurement model for financial instruments contain an explicit tainting notion or should it rely on the principle and exercise of professional judgment? Why?

We believe that the model should rely on the principle and exercise of professional judgment, though we observe that creating a high threshold for a change in business model may increase tension on whether an inappropriate number of sales are occurring in certain classification categories.

Question 13: The proposed amendments would require loan commitments, a revolving line of credit, or a commercial letter of credit (the potential creditor) to be measured on the basis of the likelihood of exercise of the commitment and the classification of the underlying loan that would be made upon exercise of the commitment. Do you agree with the proposed classification of loan commitments? If not, why? What would you propose instead?

We agree with the proposed classification of loan commitments.

Question 14: Do you agree with the initial measurement principles for financial instruments? If not, why?

We agree with the initial measurement principles for financial instruments, though we would prefer that the Board provide more application guidance for the proposed paragraphs 825-10-30-4 to 30-6. The Board should also consider whether a clearly de minimus or insignificant incentive requires application of the guidance in proposed paragraph 825-10-30-4, and should also address the lack of readily available fair market value information for smaller entities in applying the guidance.

Question 16: Should financial liabilities subsequently be measured at amortized cost, unless certain exceptions are met? If not, why?

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We believe that financial liabilities should subsequently be measured at amortized cost as indicated in the proposed amendments.

Question 18: The proposed amendments would require financial assets measured at amortized cost that are subsequently identified for sale to continue to be classified and measured at amortized cost less impairment and would prohibit recognition of the gain, until the sale is complete. Do you agree with the proposed classification and measurement requirements? If not, why?

We agree with the proposed requirements.

Question 19: The proposed amendments would provide a practicability exception for measuring equity investments without readily determinable fair values that do not qualify for the practical expedient in paragraph 820-10-35-59 (that is, net asset value per share expedient) and a one-step impairment model for all equity investments subject to the practicability exception. Do you agree with the proposed amendments? If not, why?

We agree with the practicability exception. We also believe that adding implementation guidance and illustrations would be beneficial.

Question 20: Should an entity evaluate the need for a valuation allowance on a deferred tax asset related to a debt instrument measured at fair value with qualifying changes in fair value recognized in other comprehensive income separately from the other deferred tax assets of the entity (rather than combined and analyzed together)? If not, why?

We do not believe that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to a debt instrument measured at fair value with qualifying changes in fair value recognized in other comprehensive income separate from other deferred tax assets. Conceptually, we do not think there is a strong argument to identify a single component of the deferred tax asset when considering whether a valuation allowance is necessary.

Question 21: Under the amendments in this proposed Update, hybrid financial assets would not be required to be analyzed for bifurcation under Subtopic 815-15 and would be assessed in their entirety on the basis of the proposed classification requirements. In contrast, hybrid financial liabilities would be assessed for bifurcation and separate accounting under Subtopic 815-15, and the financial liability host contract would be subject to the proposed amendments. Do you agree with this proposal? If not, why? What would you propose instead?

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We agree with this proposal.

Question 22: The proposed amendments would require reclassification of financial assets when a change in business model occurs and prescribes how those changes should be subsequently accounted for. Do you agree with the proposed amendment on reclassifications? If not, why?

We agree with the proposed amendment on reclassification. We believe that additional implementation guidance and illustrations would be beneficial in this area, specifically with respect to the presentation of assets that have a business model reclassification during the period, but are sold prior to the end of the period.

Question 29: Do you agree with the proposed disclosure requirements? If not, which disclosure requirement would you change and why?

Overall, we agree with the proposed disclosure requirements. We are concerned regarding the cost to audit the disclosures proposed in paragraph 825-10-50-34. The value to users of providing fair value hierarchy information for parenthetically disclosed fair value information is not apparent. Entities would need to expend resources to obtain and track the information and this could be burdensome for the smaller institutions as the information may not be available by deposit type. The cost to audit this information is, in our view, disproportionate to the benefit received by financial statement users.

Question 30: Should an entity be permitted to early adopt only the proposed presentation requirements related to changes in instrument-specific credit risk for hybrid financial liabilities that would qualify for the fair value option under the proposed requirements? If not, why?

We do not believe that an entity should be permitted to early adopt the proposed presentation requirements related to changes in instrument-specific credit risk for hybrid financial liabilities that would qualify for the fair value option under the proposed requirements. The inclusion of this information may be challenging to users and it would affect comparability to prior periods presented as well as across industries as not all entities would elect to early adopt this portion of the proposed amendments. We believe that all the proposed amendments should be adopted simultaneously.

Question 31: Should the effective date be the same for both public entities and nonpublic entities?

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We believe that the effective date for nonpublic companies should be a year later than the effective date for public companies.

Question 32: How much time is needed to implement the proposed guidance?

We believe that, at a minimum, entities would need approximately two to three years to implement the proposed guidance.

Question 33: Are the transition provisions in this proposed Update operable? If not, why?

While we believe the transition provisions are generally operable, we are concerned about the comparability to prior periods in the year of adoption. We appreciate that the transition provision provides for a more simplified approach that would mitigate the cost of implementation on behalf of the preparers; however, given the fundamental changes to the line items and structuring of the balance sheet caused by this proposal, it is unclear to us how entities will prepare their balance sheet under a cumulative-effect adjustment in the first year the guidance is effective. Users of the financial statements will likely find it difficult to compare periods, even with the proposed disclosures that are a part of the transition provisions. If the Board chooses to retain the proposed transition provisions, we recommend that additional guidance be included on how, in practice, the balance sheet should be prepared in the period of adoption. The Board could also consider modifying the transition provisions to be adopted retrospectively for the earliest period presented to improve comparability.

Question 34: The proposed amendments would require investments that qualify for the equity method of accounting in Subtopic 323-10, Investments – Equity Method and Joint Ventures – Overall, to be subsequently measured at fair value with changes in fair value recognized in net income if the investment is held for sale at initial recognition. Are the proposed indicators/conditions operable? If not, why? What would you propose instead?

The proposed indicators/conditions appear to be overly broad, as nearly any equity method investment could be considered to meet the held for sale criteria. Additionally, the broad indicators would limit comparability among entities by providing a de facto fair value option for equity method investments. For instance, in the real estate industry, where equity method investments are frequently made alongside controlled investments in similar underlying assets, the proposed indicators/conditions would result in a different measurement basis for similar assets in the same financial statements. Equity method investments are also prevalent in the healthcare industry, and the broad held for sale conditions may result in a lack of comparability of similar equity method investments both within an entity's financial statements and between the

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financial statements of different entities in the same industry. As discussed in our responses above, we also are concerned about small entities bearing the incremental costs required for fair value measurement and disclosure if the proposed guidance results in equity method investments being measured at fair value. We recommend that the Board narrow the scope of the indicators/conditions so that only equity investments to be sold in the relatively near term are considered held for sale.

Question 35: The proposed amendments would change the current two-step impairment model for equity method investments to a one-step impairment model for all equity instruments. Do you agree with the proposed one-step equity impairment model? If not, why? What would you propose instead?

Our understanding of the impairment model would be that the qualitative indicators in proposed paragraph 323-10-35-31A would be assessed, and if an entity determined an investee was impaired, the impairment loss should be based on the fair value of the equity method investment, similar to the proposed model in paragraphs 825-10-35-18 and 35-19. Proposed paragraph 825-10-35-31B does not prescribe how the amount of impairment loss should be determined and we recommend linking the guidance in proposed paragraphs 825-10-35-18 and 35-19 to proposed paragraph 825-10-35-31B to ensure clarity.

Question 36: Do you agree that the current portfolio-wide option for not-for-profit entities, other than health care entities, to account for their equity method investments at fair value should be retained? If not, why? Should that option also be made available to not-for-profit health care entities that are within the scope of Topic 954, Health Care Entities?

We agree that the current portfolio-wide option for not-for-profit entities should be retained. We further believe that this option should also be made available to not-for-profit health care entities. As noted in our response to Question 34, the held for sale indicators are drafted so broadly that an entity has a de facto option to designate equity method investments as held for sale and account for them at fair value. If the Board retains the proposed held for sale indicators, we would recommend that the Board expand the option to measure any equity method investment at fair value through net income.