September 17, 2021

Technical Director
Financial Accounting Standards Board
401 Merritt 7
Norwalk, CT 06856-5116

Re: Invitation to Comment *Agenda Consultation*

Dear Ms. Salo:

The AICPA's Financial Reporting Executive Committee (FinREC) appreciates the opportunity to comment on FASB's Invitation to Comment (ITC) *Agenda Consultation*. FinREC applauds the outreach FASB did prior to issuing the ITC, as evidenced by the robust thought that appears in the document.

FinREC is the senior AICPA committee authorized to speak on financial reporting matters. FinREC represents a diverse group of constituents. Current FinREC members include preparers, auditors, an academic, a valuation specialist, and a user of financial statements. In preparing to respond to FASB's ITC, we considered what projects would be most meaningful to all of our members, as well as those that are most achievable in a reasonable period of time. Importantly, we did not attempt to offer ideas that would completely fill FASB's future agenda – for example, we believe there always needs to be room to address emerging accounting issues. Likewise, we do not offer comments on all potential projects listed in the ITC. Instead, we have focused our comments primarily on the three areas we identified as the highest priority items: crypto assets, key performance indicators and government grants for business entities.

For certain of our suggested priority projects listed below, FinREC attempted to offer FASB a reasonable starting point that realistically could result in timely standards that move the proverbial needle to (1) help better meet the needs of users and (2) solve some challenges in financial reporting. Our belief is incremental focus that can be done timely is a better outcome than broad, complicated projects whose twists and turns will assuredly result in very long-term projects that may have no end, especially in topical areas experiencing high-speed innovation.

In order to facilitate FASB's review of our response, we have ordered our comments consistent with the questions included in the ITC. Those relating to our three priority areas are included first, with responses to certain other questions included at the end.

Crypto Assets

Question 11: Preparers and practitioners—Does your company (or companies that you are involved with) hold significant digital assets, such as crypto assets? What is the purpose of those holdings?

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FinREC Response: We observe on an increasingly frequent basis that companies are using and exploring the use of digital assets in their business transactions. While some entities who accept digital assets as payment for goods and services immediately convert those assets to cash, others hold those assets past a reporting period date. In addition, public accounting firms receive a growing number of complex financial reporting questions related to crypto assets. In summary, this area continues to evolve, and the transactions are now/anticipated to be material to the overall financial reporting system.

Question 12: If the Board were to pursue a project on digital assets, which improvements are most important, what types of digital assets should be included within the scope, and should this guidance apply to other nonfinancial assets?

FinREC Response: We believe (and observe that many others believe) that the application of current GAAP too often fails to convey the economic substance of crypto asset transactions, and too often results in counter-intuitive accounting conclusions. Therefore, we suggest that FASB has an opportunity to improve the usefulness of financial reporting on this topic.

We recommend that FASB embark on a two-phase project. We believe that the first phase, though challenging, is achievable in a somewhat expedited time frame. The second phase would include multiple important topics that need standard-setting attention, but our experience suggests this will be extremely challenging for FASB and will by necessity take more time to complete.

Based on the work of our Digital Assets Working Group and our related Practice Aid that offers accounting and auditing guidance, FinREC offers the following thoughts on how FASB might tackle this topic efficiently and effectively. Items I, II, and III are our recommendations for the phase one effort; item IV highlights a phase two effort.

I. Scope

Scoping this topic is a great challenge, as FASB has acknowledged. There is significant diversity in how "cryptocurrencies" or "crypto assets" are referred to by various practitioners, regulators, and others. FinREC believes the following scope[1] is achievable from a standard setting perspective.

A crypto asset is a specific type of asset that has all of the following characteristics:

a. It is recorded on a distributed ledger that uses cryptography for security;
b. It is not issued by a jurisdictional authority (for example, a sovereign government);
c. It does not give rise to a contract between the holder and another party.

[1] Ideas primarily sourced from the AICPA Digital Assets Practice Aid, IFRS Interpretative Committee Agenda Paper 12, and Japanese GAAP.

d. It is generally recognized as having value that is not derived from or related to any specific entities, goods, or services

Crypto assets are often intended to be used as a medium of exchange and/or investment. They are usually not considered a security under the US Securities Act of 1933 or the Securities Exchange Act of 1934.

The following assets are not crypto assets within this proposed scope:

a. Fiat currencies;
b. Assets denominated in fiat currencies;
c. Prepaid cards (tickets, tokens) issued in exchange for prepayment for goods or services;
d. "Points" issued based on sales or use of goods or services or for visits to stores;
e. Non-Fungible Tokens (NFTs)
f. Stablecoins

This guidance should not apply to crypto assets issued by the entity itself, its parent, subsidiaries, affiliates or related parties.

Bitcoin, Bitcoin Cash and Ether are examples of crypto assets in the scope of this guidance.

II. Measurement

Crypto assets currently are considered intangible assets subject to the requirements of ASC Topic 350. FinREC offers two broad considerations on whether crypto assets should be defined as a separate category of assets (Option A below) or whether such assets should be defined as a kind of intangible asset under current GAAP (Option B below). We believe both options are worth FASB's exploration, but we observe that Option B is an incremental approach that could result in a timelier standard.

Under each category, FinREC believes that FASB should explore with stakeholders if fair value should be required or optional when a liquid[2] market exists. Therefore, we offer our thoughts on both, titled as "Sub-Options" within each category.

Option A - crypto assets are a <u>separate</u> category of assets

At the balance sheet date, a crypto asset held by an entity on its own behalf (that is, excluding those held on behalf of others) should be measured as follows.

<u>Sub-Option 1 (fair value required):</u> If a liquid market exists for the crypto asset, such crypto asset should be measured using the fair value as defined by ASC Topic 820. Any

[2] FinREC uses the word *liquid* to convey plain English intent without debating terms used in GAAP.

adjustment to the carrying amount of the asset should be recognized as a gain or loss within the statement of financial performance.

<u>Sub-Option 2 (fair value optional):</u> If a liquid market exists for the crypto asset, the entity can make an election to carry such crypto asset at fair value as defined by ASC Topic 820. If the entity makes such election, any adjustment to the carrying amount of the asset should be recognized as a gain or loss within the statement of financial performance. The election can be made independently for each class of identical assets. The election can be made at the time the entity first acquires a crypto asset, and FASB should consider also allowing for such election at a later date. Once the election is made for a specific crypto asset, it cannot be revoked unless there is no longer a liquid market for such asset.

<u>The text below applies to both Sub-Option 1 and Sub-Option 2:</u>
If a liquid market does not exist for the crypto asset, such asset should be accounted for at cost. It should be tested for impairment at the end of each reporting period if events or changes in circumstances indicate it is more likely than not that the asset is impaired. If there is substantial evidence of recoveries of impairment losses in later interim periods of the same fiscal year, such recoveries should be recognized as gains, in the amounts not to exceed previously recognized losses. If impairment is recognized on a crypto asset as of the end of the fiscal year, the impaired value becomes the new cost of the asset.

A liquid market (as defined in ASC 820-10 Glossary) exists for the crypto asset when there is a market in which transactions for the crypto asset take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

If a liquid market previously existed but no longer exists, for crypto assets previously carried at fair value, the fair value as of the last date the liquid market was in existence becomes the new cost basis.

Option B - crypto assets are a specific type of an <u>intangible asset</u>

At the balance sheet date, an intangible asset that meets the definition of a crypto asset in scope of this guidance that is held by an entity on its own behalf (that is, excluding those held on behalf of others) should be measured as follows:

<u>Sub-Option 1 (fair value required):</u> If a liquid market exists for the crypto asset, such crypto asset should be measured using the fair value as defined by ASC Topic 820. Any adjustment to the carrying amount of the asset should be recognized as a gain or loss within the statement of financial performance.

<u>Sub-Option 2 (fair value optional):</u> If a liquid market exists for the crypto asset, the entity can make an election pursuant to ASC 825-10-25 to carry such crypto asset at fair value. If the entity makes such election, any adjustment to the carrying amount of the asset should be recognized as a gain or loss within the statement of financial performance. The election can be made independently for each class of identical assets. Although the guidance in ASC 825-10-25 allows the election to be made only at the time the entity first

acquires an asset, FASB should consider also allowing for such election at a later date for crypto assets. However, once the election is made for a specific crypto asset, it cannot be revoked unless there is no longer a liquid market for such asset.

The text below applies to both Sub-Option 1 and Sub-Option 2:
If a liquid market does not exist for the crypto asset, such asset should be accounted for as an indefinite-life intangible asset in accordance with Topic 350. In particular, it should not be amortized but should be tested for impairment in accordance with ASC 350-30-30-1 annually or more frequently if events or changes in circumstances indicate it is more likely than not that the asset is impaired.

Also, FinREC believes that the current model in Topic 350 should be amended to allow crypto assets accounted for at cost to be written back up to cost to reflect subsequent impairment recoveries, thus being an exception to the broad requirements on impairment of intangible assets. Our sense is that stakeholders will find this approach more useful than the current permanent write-down approach.

III. Disclosures

FinREC encourages FASB to engage with users on their information needs related to this scope. We identified two paths worth exploring:

Option A: Where fair value is required or used (initial measurement or impairment), entities should provide information about the inputs used and the leveling decisions.

Option B: All crypto assets (as scoped herein) would require that an entity disclose the above fair value information regardless of the measurement basis used. This would include those entities that 1) do not elect fair value as a measurement basis and 2) do not have a liquid market.

IV. Receivables/payables of crypto assets, and other more comprehensive phase two topics

One of the more challenging current topics is crypto asset lending/borrowing activities and the related derecognition considerations. For practical reasons FinREC recommends that this topic not be addressed at the same time as the above topics. Therefore, FinREC's recommendation is that this topic, along with other complex ones, should be considered for a phase two effort. Our Digital Assets Working Group has identified many complexities on this and other topics, and we would be happy to share these observations with your staff.

Financial KPIs or Non-GAAP Metrics

Question 14: Are there common financial KPIs or metrics—either widely applicable to all companies or industry specific—that would provide decision useful information if they were defined by the FASB? Please explain.

FinREC Response: We believe that earnings before interest, taxes, depreciation, and amortization (EBITDA) and free cash flow are financial KPIs commonly used across many industries, and that having standard GAAP definitions would provide transparency and consistency to users of financial statements. We recommend that the GAAP definitions include a description of the components of EBITDA and free cash flow, and that the components also be disclosed if such metrics are included in the audited financial statements.

We believe that including standard definitions will provide a known/common starting point for these widely used financial KPIs, and potentially result in less diversity as some companies may decide not to further deviate from the defined KPIs. We acknowledge that establishing a GAAP definition of EBTIDA and free cash flow may result in certain complexities (for example, deciding whether to include interest on financing leases and pension liabilities as interest expense). However, we also note that there are common definitions in existence today among the user and preparer communities that can and should be leveraged, for example in standard-form debt covenants, and believe that appropriate transition provisions will allow for convergence to the extent that an individual entity's past practice is different.

As FinREC believes that additional transparency in understanding management's judgements is important to users of financial statements, we recommend that the FASB consider a secondary project to require management to communicate its framework for determining key metrics such as core vs. noncore and recurring vs. nonrecurring items. As establishing common definitions for these items would be very challenging, we believe it would be more beneficial to focus the project on gaining insight into management's judgment by providing parameters for the disclosure of how significant key items are defined and applied by a company. The disclosure of these key items would be similar to the requirements for segment reporting, which also provides transparency into how management assesses company performance.

Although FinREC expressed concerns with the IASB project on the reporting of management performance measures, in particular with the residual approach taken for determining operating activities, we recommend that if FASB adds either of the suggested financial metric projects to its agenda that it monitor the IASB project to ensure convergence where possible and appropriate.

Question 15: If the FASB were to define certain financial KPIs or metrics, should all companies be required to provide those metrics or should providing those metrics be optional?

FinREC Response: If EBITDA and free cash flows are defined as recommended in our response to Question 14, we believe providing these metrics should be optional. We believe that each company should be allowed to determine if the use of EBITDA and free cash flows would be beneficial to its financial statement users. However, if the Board believes the defined financial KPIs should be required disclosures for all companies including those that currently do not utilize them, FinREC recommends that the Board first perform outreach to obtain a better understanding of the needs of users of public companies, private companies, and not-for-profit entities, and related potential costs to preparers of financial statements.

If the FASB adds the suggested project to require management to communicate its framework for defining and applying key metrics, FinREC again recommends that the Board perform outreach to understand potential benefits to financial reporting and costs to prepare, in particular for private companies and not-for-profit entities.

Government Grants for Business Entities

Question 16: If the Board were to pursue a project on the recognition and measurement of government grants, should the FASB leverage an existing grant or contribution model (such as the models in IAS 20 or Subtopic 958-605) or develop a new model? If you prefer leveraging an existing model, which would be most appropriate and why? If the FASB were to develop a new model, what should the model be?

FinREC Response: We believe the time has come for FASB to develop guidance on accounting for government grants focused on business entities. We have recently witnessed multiple cycles of government assistance to business entities, and believe it is likely that will continue, especially as government signals it intends to offer more support to “critical” industries.

We believe that both the IAS 20 and Subtopic 958-605 models are robust and provide meaningful information to users of the financial statements. Therefore, we believe FASB could utilize either (or elements of both) model(s) as a basis for a new standard, and does not need to recreate the wheel. We would also recommend that FASB consider the output of our predecessor committee AcSEC in its 1979 Issues Paper *Accounting for Grants Received from Governments,* which largely served as the basis for what is now IAS 20.

Question 17: The FASB has encountered challenges in identifying a project scope that can be sufficiently described for government grants. If the Board were to pursue a project on the recognition and measurement of government grants, what types of government grants should be included within the scope and why (for example, narrow or broad scope)?

FinREC Response: Similar to FASB’s recent decision on its related disclosures project, we believe that the scope should be direct government assistance (for example, in the form of cash, land, and PP&E grants/contributions). This important but narrow focus should be achievable in a timely manner.

Examples of items that would be outside the scope of this initial phase are various tax incentives and abatements, and government services. Our reason for excluding such transactions is solely practical – the scoping is incredibly challenging and would impede issuing a timely standard. We would support FASB engaging on these aspects in a phase 2 effort.

Other FinREC Comments on the ITC

Overall Questions

Question 5: The objective of the ITC and the related 2021 Agenda Consultation process is to ensure that the FASB continues to allocate its finite resources to standard-setting activities that fulfill its primary mission of improving financial accounting and reporting standards and that are of the highest priority to its stakeholders. Therefore, feedback on the prioritization of projects on the FASB's technical agenda (see Appendix A) would be helpful. Do you have any feedback on the FASB's technical agenda, including the following:

a. *Which projects on the FASB's agenda should the Board prioritize completing? Please explain.*
b. *Which projects, if any, should the Board deprioritize or consider removing from the agenda? Please explain.*
c. *Which projects, if any, need to be redefined to improve the objective and/or scope? Please explain.*

FinREC Response: We believe that FASB should continue to prioritize its efforts to improve subsequent accounting for goodwill. In addition, we also support FASB's continuing efforts to improve segment reporting and as further discussed below in our response to Question 23, distinguishing liabilities from equity.

As discussed above in our response to Question 14 and below in our response to Question 6, we support FASB focusing its financial performance reporting project on disclosures related to how management determines core vs. noncore and recurring vs. nonrecurring items.

As we noted earlier, FASB's agenda must always allow for flexibility to address emerging issues. For example, FinREC recently submitted an agenda request on the accounting for funding credit balances and employer contributions receivable in defined benefit pension plans, and employee and employer contributions receivable for a single employer defined contribution plan. Likewise, the AICPA Insurance Expert Panel recently submitted a complex technical inquiry to FASB staff related to the implementation of the recognition and measurement guidance for market risk benefits within FASB ASU 2018-12. We believe it would be a valuable use of FASB's time and resources to address both of these requests.

Disaggregation of Financial Reporting Information

Question 6: Greater disaggregation and granularity of the types of financial reporting information described in Chapter 1 have been identified as decision useful to investors. The following insights would be helpful to the FASB when considering this area:

a. *Investors and other financial statement users—Which, if any, of the areas described in Chapter 1 should be a top priority for the FASB to consider requiring greater disaggregation—on the income statement, the statement of cash flows, or the notes to financial statements? Would this information be most useful in the* *financial statements or in the notes to financial statements? How would this information be used to analyze a company and make capital allocation decisions?*

b. *Preparers—What requests or questions does your company receive from analysts on the areas described within Chapter 1? Please explain any requests or questions your company has received.*

FinREC Response: As noted above in our response to Questions 5 and 14, FinREC would support a project to disclose how management determines core vs. noncore and recurring vs. nonrecurring items.

Distinguishing Liabilities from Equity

Question 23: Stakeholders noted many challenges in applying the liabilities and equity guidance, but they had mixed views on how the Board should improve the accounting for financial instruments with characteristics of equity. The Distinguishing Liabilities from Equity Phase 2 project is intended to align the two existing indexation models in Topic 480 and Subtopic 815-40. Should the Board continue pursuing this project in its current scope and objective, or does the Board need to reevaluate this project? Please explain why or why not and if the project scope and objective need to be reevaluated, what should the approach be?

FinREC Response: We agree that the Board should continue pursuing the current project to align the two existing indexation models. We support FASB's approach of addressing narrow issues that will improve the accounting and reporting for complex financial instruments rather than a more holistic "clean sheet" approach. In that vein, we would support a project to incorporate a concept similar to the SEC's guidance on mezzanine presentation into the Codification. Providing for a mezzanine classification could relieve some of the pressure inherent in the current debt vs. equity assessments.

Improvements to FASB Standard-Setting Processes

Question 25: Which, if any, of the FASB processes described in Chapter 4 of this ITC could be improved? Please explain your rationale for each, including the following:

a. *Why that process needs improvement*
b. *How the FASB should improve that process*
c. *What the urgency is of that process improvement*

FinREC Response: We believe the following two areas would represent shorter term projects that would significantly improve the standard-setting process and understandability of the Codification:

<u>Standardizing Language Used to Describe Transition Requirements</u>

Stakeholders have no doubt appreciated the standard-by-standard considerations FASB gives to allow for a commonsense approach to the transition requirements of new standards. However, for those of us who implement or audit many of those standards, we encourage FASB to consider if it can offer more consistent language for transition requirements across all standards. For example, the term "modified retrospective" is used in multiple standards, including ASC 606 and ASC 842, to describe differing transition methodologies. While we agree that different standards may require different transition methods, we believe that standardizing the terminology used will improve the understandability and thus the adoption process. Additionally, our bias is for FASB to strive for substantively consistent transition requirements wherever possible.

Improving the Understandability of the Codification - Incorporating Basis for Conclusions and published staff inquiries in the Codification

We note the Basis for Conclusions to each new standard includes a significant amount of information that explains the basis for the decisions made by FASB in finalizing the guidance in that standard. Although nonauthoritative, this information is an invaluable resource in understanding the intent of the standard, and thus how to apply it. We would strongly support a project that would result in incorporating the information from the Basis for Conclusions into the Codification. Currently, the only way to access this information is to go to the individual Accounting Standards Update, which is a cumbersome process. We recommend adding a section to each Codification Topic with a distinct numbering scheme, similar to how SEC guidance is incorporated in the S sections, to capture this nonauthoritative information. Ideally, a second phase project would link or cross-reference the information in the Basis for Conclusions to the guidance in the Codification as well as published staff inquiries.

Members of FinREC and AICPA staff would be pleased to discuss any of these comments at your convenience.

Sincerely,

Angela J. Newell
Chair
FinREC