AICPA® PCPS
Private Companies Practice Section

Summer 2017

Technical Issues Alert

Information on technical issues affecting small businesses and the CPAs who serve them.

Timely Topics at TIC's Meetings with FASB and PCC

TIC meets regularly with standard setters to learn about projects in development and share information on practice experiences and concerns. At TIC's most recent liaisons with the Financial Accounting Standards Board and the Private Company Council, the discussions covered both implementation issues with existing standards and guidance in development.

The definition of various entities. TIC noted that there are multiple definitions throughout the FASB codification of the terms *public business entities* (PBEs) and *public, non-public* and *private entities*, and discussed the uncertainty and unnecessary complexity that can result. In addition, while not-for-profits are not technically PBEs, TIC discussed instances of confusion about those that are conduit debt obligors.

Update 2016-13—Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. TIC members offered recommendations on potential additional implementation guidance related to calculations and quantification of some disclosures required under this standard, noting that lengthy credit quality disclosure can be burdensome for private entities. There is a FASB in Focus Fact Sheet on this topic.

FASB ASC 740 practice issues. A TIC guest representing a group of interested firms reviewed several areas where practitioners are seeing implementation issues with this standard on accounting for income taxes, including:

- Measurement "step 2" issues related to FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes,* and possible simplification steps.

- Intra-period allocation for full valuation allowance companies, and restatements related to the exception for taxable gains outside continuing operations as in discontinued operations, OCI, and equity.

- Accounting for nondeductible goodwill, and possible simplifications that would address inconsistencies in the standards.

Readily determinable fair value. TIC discussed confusion about the definition of this term in practice, particularly for employee benefits plans and not-for-profits. TIC called for potential additional guidance on the definition in light of the issuance of ASU 2015-10 *Technical Corrections and Improvements*. The Financial Reporting Executive Committee plans to issue some Technical Practice Aid Q&As that will provide additional clarification.

Proposed Accounting Standards Update—Compensation—Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting. TIC has offered recommendations for disclosure relief in this area in its comment letter on this ED and on the *Agenda Consultation Invitation to Comment*. In its meetings with the FASB and the PCC, TIC members noted that many

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Future Meetings

TIC meetings offer local practitioners the chance to provide their unique perspectives in the standard-setting process. All CPAs are invited to attend. Contact Kristy Illuzzi, CPA, TIC Staff Liaison, at the AICPA at (919) 402-4057 to learn about attending or receiving information on upcoming meetings.

The next TIC meetings will be held:
- September 26 and 27, Coronado, CA
- November 14 and 15, Savannah, GA (TIC's annual liaison with ARSC)
- January 17 and 18, San Juan, PR (TIC's annual liaison with the ASB)
- May 8 and 9, TBD (TIC liaison with PEEC)

The PCPS Technical Issues Committee (TIC) provides standard setters with the unique perspective of local CPA firms on accounting, auditing and reporting issues. We hope these highlights of issues that affect local firms will help you, your firm or your group to participate in the standard-setting process.

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complex disclosures are of little value to private company financial statement users. TIC outlined possible simplifications, particularly for forfeitures, and discussed some improvements regarding profit interest awards related to LLCs and partnerships.

Proposed Accounting Standards Update—Debt (Topic 470) Simplifying the Classification of Debt in a Classified Balance Sheet (Current versus Noncurrent). While TIC appreciated some of the proposed modifications in this ED, its comment letter expressed concerns in two areas: the required period for a waiver and debt refinancings. In its meetings, TIC discussed banks' reluctance to issue waivers for a year and a day in certain cases (particularly to smaller, nonpublic entities), which would be necessary under the proposal. TIC also pointed out the problems that the proposed debt refinancing requirements could cause for many private companies, particularly contractors and construction companies. Suggested changes in balance sheet classification based solely on contractual terms regardless of refinancing after the balance sheet date would no longer represent the true maturity terms at the date of the issuance of the financial statements. TIC feels that users such as creditors, regulators and licensing agencies may be required to redesign and rethink their application and compliance processes to address the changes expressed in the exposure draft. FASB members noted that the board's planned additional research on this proposal will include outreach to construction licensing boards.

Proposed Accounting Standards Update—Inventory (Topic 330): Disclosure Framework—Changes to the Disclosure Requirements for Inventory. In its meeting with the PCC, TIC noted that while it generally supported this ED (read TIC's comment letter), it was concerned that the use of the Retail Inventory Method (RIM) could force companies to reveal proprietary information. ■

Answers Please!

In this issue, we introduce a regular feature highlighting answers to questions received by the AICPA Center for Plain English Accounting. Below is a recent question related to debt covenant violations that the AICPA has received through its technical inquiry service that we thought you might find helpful. Note that this response relates to the guidance under current U.S. GAAP.

Inquiry: A client violated a loan with a covenant requiring audited financial statements by a set date. Is failure of this covenant treated the same way as financial ratio covenants, and would therefore result in the debt being reclassified to current on the balance sheet?

Response: A failure of a covenant requiring audited financial statements by a specified date should be treated the same as any other covenant violation. Assuming that failing a covenant results in the loan holder being able to call the debt immediately, then the debt should be classified as current.

The AICPA has some additional guidance in AICPA Technical Q&A3200.17 as well, which relates to a situation where a waiver has been obtained from the lender and relates to if that violation and subsequent waiver require disclosure. As a reminder, a waiver for one year from the balance sheet date would not be sufficient, as one year exactly would still be considered a current liability. The terminology used in current guidance has either been "more than a year" (which is used in the AICPA Technical Q&A) or "at least a year and a day", both of which address the point that the waiver date would need to extend far enough into the future to result in the debt not being current as of the balance sheet date. If the debt does need to be classified as current and there is no waiver obtained, you may also need to revisit the going concern analysis/documentation to make sure that any required changes are made.

TIC Supports Simplified VIE Guidance for Private Companies

In its comments on the Proposed Accounting Standards Update, *Consolidation (Topic 810): Targeted Improvements to Related Party Guidance for Variable Interest Entities*, TIC applauded efforts to simplify existing guidance for variable interest entities (VIEs), which can be tough to implement in practice. This is especially true when entities are under common control, which is often the case with private companies. TIC recommended that private companies should be allowed but not required to apply VIE guidance to legal entities under common control, since consolidated financial statements often don't suit the needs of banks and other private company financial statement users. TIC supported the proposal to consider indirect interests held through related parties under common control on a proportional basis rather than as the equivalent of a direct interest in its entirety, which is now required. In TIC's opinion, this would reduce the chances that a decision maker that is an agent could be considered the primary beneficiary

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of a VIE, and prevent attempts to avoid consolidation rules. TIC also approved dropping the related party tie-breaker test for private entities, which don't often use it. TIC urged the board to allow the guidance to become effective for private companies even if further revisions are needed for any proposed requirements for public business entities. ■

The Latest on Revenue Recognition

Want to know the latest developments related to the Financial Accounting Standards Board's revenue recognition project? Or find new implementation information or opportunities to comment on related guidance? Turn to the AICPA Financial Reporting Center's site devoted to revenue from contracts with customers. ■

New Comment Deadline for Important ED on EBP Audits

The comment deadline has just been extended for an Auditing Standards Board ED that would create significant changes in practice. *Forming an Opinion and Reporting on Financial Statements of Employee Benefit Plans Subject to ERISA* would establish specific auditing standards for these plans. Practitioners have more time to voice their opinions because the comment deadline has been extended to September 29. In its comments on the ED, TIC voiced strong opposition to a proposed reporting requirement for findings from procedures. The findings would be attached to the entity's Form 5500, even if they are not disclosed in the auditor's opinion or a separate deliverable. Including specific findings in the audit report would cause confusion about the auditor's conclusion on the financial statements, in TIC's opinion. It could also expose plan sponsors, plan administrators and auditors to additional risk without enhancing audit quality. Instead, TIC recommended that auditors be required to communicate the findings to those charged with governance of the plan in a separate letter as required under standards in AU-C sections 260 and 265.

The ED also calls for auditors to perform substantive procedures in some cases no matter whether there is a risk of material misstatement in those areas. TIC noted that this would extend the auditor's responsibility beyond the normal scope and create unnecessary costs for plan sponsors and participants. TIC also pointed out other proposals that could result in additional costs or unintended consequences.

TIC is not sure that adding a listing of all the procedures performed to the report would be appropriate. Although it may help a user of those financial statements to understand what the audit encompasses, TIC does not believe that including this information in the auditor's report will necessarily help to improve audit quality. TIC believes that audit reports should not be designed as a checklist for audit procedures performed, but rather for reporting on the overall results of the audit of the Plan financial statements. Given the complexity of the proposed changes, TIC called for a delayed effective date to allow sufficient time for plan sponsors and auditors to become familiar with the requirements. However, TIC endorsed certain other aspects of the proposed new reporting model for these engagements as outlined in the ED. ■

TIC Meets with the GASB

TIC's annual meeting with members of the Governmental Accounting Standards Board and staff addressed several GASB projects under way, as well as recent or expected EDs.

Certain Disclosures Related to Debt, Including Direct Borrowings and Direct Placements—An Amendment of GASB Statements No. 34 And No. 38. TIC members offered preliminary thoughts on this recently issued ED. The comment deadline is September 15.

Financial Reporting Model Improvements—Governmental Funds. TIC and GASB representatives discussed responses to an Invitation to Comment (ITC) on this project, which aims to make improvements to GASB Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, and other guidance related to the reporting model. TIC members offered perspectives on how the approaches under consideration—near-term, short-term, and long-term—would affect smaller governments. A TIC member attended one of the public hearings earlier this summer where the three different models were discussed in detail. TIC also volunteered to recommend clients willing to participate in field studies of each approach. A preliminary views document is expected in the third quarter of next year.

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Other Postemployment Benefits (OPEB) Implementation Issues. TIC members reviewed some of the challenges clients face in implementing this standard, including higher actuary costs. An ED for an implementation guide was issued on June 28. Comments are due by September 25.

Revenue and Expense Recognition. This project covers recognition of revenues and expenses related to nonexchange, exchange and exchange-like transactions, including guidance for exchange transactions not included in existing standards. It does not encompass accounting for governmental funds and the financial reporting model, financial instruments or capital asset recording. An ITC is expected early next year.

Capitalization of Interest Cost. In discussing this GASB project, TIC members described issues related to the capitalization of construction period costs, including potential diversity between GAAP and regulatory reporting, if certain changes are made to existing guidance, as well as possible challenges for hospitals and public universities.

Conduit Debt—Reexamination of Interpretation 2. As GASB considers the necessity of updated guidance in this area, TIC members provided insights on their clients' experiences and recommendations on possible changes.

Going Concern Disclosures—Reexamination of Statement 56. TIC received information and provided feedback on this preliminary project.

TQAs on Use of Inappropriate Accounting Standards. TIC discussed with GASB representatives a new set of *AICPA Technical Questions and Answers* issued in response to recent questions from AICPA members auditing governmental entities, including Indian tribes. Question and Answer (Q&A) section 9160.31–.35 provides nonauthoritative guidance that addresses reporting on financial statements developed using an inappropriate set of standards. The TQAs also discuss whether an entity is a state or local government for purposes of determining whether it is using the appropriate set of accounting standards, and how to report on the entity's financial statements when the entity elects to follow either a different set of standards or a special purpose framework. ■

TIC Advocacy in Action

- TIC made contributions to an Auditing Standards Board comment letter on a proposed IAASB ED, International Standard on Auditing 540 (Revised), *Auditing Accounting Estimates and Related Disclosures*. A TIC member was a member of the task force that drafted the ASB's comment letter, offering the small firm perspective. The ED proposed what the IAASB says are significant changes in how auditors evaluate accounting estimates and related disclosures.
- TIC members offered feedback during the drafting of the AICPA comment letter on the Government Accountability Office's proposed changes to *Government Auditing Standards (the* Yellow Book). The summary to the ED lists the major proposed changes.
- A TIC member offered feedback to the AICPA Healthcare Expert Panel on recent issues related to the new standard on revenue recognition related to healthcare entities. ■

ASB Issues SAS No. 133 on Exempt Offering Documents

The Auditing Standards Board issued SAS No. 133, *Auditor Involvement With Exempt Offering Documents* (AICPA, *Professional Standards*, AU-C sec. 945), to address the auditor's responsibilities with respect to securities offerings exempt from registration under the Securities Act of 1933 and to franchise offerings. AU-C section 925, *Filings With the U.S. Securities and Exchange Commission Under the Securities Act of 1933* (AICPA, *Professional Standards*), addresses securities offerings that are subject to registration under the Securities Act of 1933. Before the issuance of SAS No. 133, the AICPA provided best practices on municipal securities issuances in industry-specific auditing guidance in the AICPA Audit and Accounting Guides, *State and Local Governments* and *Health Care Entities*. SAS No. 133 amends AU-C section 560, *Subsequent Events and Subsequently Discovered Facts* (AICPA, *Professional Standards*), and AU-C section 925, and becomes effective for exempt offering documents with which the auditor is involved that are initially distributed, circulated or submitted on or after June 15, 2018. ■

Proposed Ethics Guidance

Entities Included in State and Local Government Financial Statements. A proposed interpretation from the AICPA Professional Ethics Executive Committee, *State and Local Government Entities*, includes potential changes to the independence rules for these entities. Comments are due by October 16.

Long Association of Senior Personnel with an Attest Client. In developing the proposed interpretation, PEEC considered the new ethics standard Long Association of Personnel with an Audit Client of the International Ethics Standards Board for Accountants (IESBA) Code of Ethics for Professional Accountants (IESBA code). TIC does foresee some potential issues with this proposal, including additional documentation requirements. TIC plans to issue a comment letter before the September 15 deadline. ■

CAQ Issues Planning Alert for Auditors of Brokers and Dealers

To enhance audit quality and help auditors of brokers and dealers plan their 2017 audits, the Center for Audit Quality has issued the *Audit Planning Alert for Auditors of Brokers and Dealers*. The publication poses questions for auditors of brokers and dealers to consider as they plan both their audit and attestation engagements. It identifies and discusses some of the more judgmental or complex areas of both the audit and attestation engagements, including areas that have been the subject of attention and focus by the Public Company Accounting Oversight Board in its interim inspection process.

While this CAQ member alert highlights certain areas for consideration, it should not be relied upon as definitive or all-inclusive and should be read in conjunction with the applicable rules, standards, and guidance in their entirety. ■

New FAQs on OMB Audits

The Office of Management and Budget has published 24 new FAQs on Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards. ■

Former TIC Member Appointed to PCC

Jeremy Dillard, partner with Singer Lewak, LLP, and a former TIC member, has been appointed to a three-year term on the Private Company Council. Several former TIC members have served on the council, including PCC Chair Candace Wright. ■

Let Us Hear From You
If you have questions, local firm advocacy issues or suggestions for TIC, contact:

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