FASB Small Business Advisory Committee
MINUTES OF MEETING
June 5, 2009

The FASB Small Business Advisory Committee (SBAC) met at the FASB offices in Norwalk, Connecticut.

Members Present
P. Glenn Bradley
Gary M. Cademartori
Robert A. Dyson
Mark Ellis
Richard E. Forrestel, Jr.
Richard H. Gesseck
William G. Hall
Gregory P. Hanson
Dennis R. Hein
Albert G. Pastino
Neal A. Petrovich
Leonard Steinberg
Troy D. Templeton
E. Anson Thrower
Scott M. Waite
Deborah A. Wilson
Samuel E. Wilson

Members Absent
W. Stephen Holmes

Others Attending

Financial Accounting Standards Board:
Robert H. Herz
Thomas J. Linsmeier
Leslie F. Seidman
Lawrence W. Smith
Chairman
Member
Member

FASB/FAF Members and Staff
Kenneth B. Bement
Jack J. Brennan
Nicholas T. Cappiello
Paul H. Glotzer
Russell G. Golden
John Ly
Kimberley R. Petrone
Teresa S. Polley
Alicia A. Posta
Adam Van Eperen
Project Manager, FASB
Chairman, Financial Accounting Foundation
Project Manager, FASB
Project Manager, FASB
Technical Director, FASB
Postgraduate Technical Assistant, FASB
Senior Project Manager, FASB
President, Financial Accounting Foundation
Executive Director, FASB Advisory Groups
Postgraduate Technical Assistant, FASB
Report of the FASB

1. Mr. Herz provided a report on the following FASB projects and other activities:
   a. The FASB has issued:
      i. FASB Statement No. 164, *Not-for-Profit Entities: Mergers and Acquisitions*.
      ii. FASB Statement No. 165, *Subsequent Events*. Mr. Herz noted that Statement 165 introduced the concept of a date based on when financial statements are “available to be issued” for private companies, which was a suggestion by the Private Company Financial Reporting Committee (PCFRC).
      iv. FSP FAS 141(R)-1, *Accounting for Assets Acquired and Liabilities Assumed in a Business Combination That Arise from Contingencies*.

   b. The FASB will soon issue:
      i. FASB Statement No. 166, *Accounting for Transfers of Financial Assets*, which will eliminate the concept of qualified special-purpose entities.
      ii. FASB Statement No. 167, *Amendments to FASB Interpretation No. 46(R)*, which changes how a company determines when an entity that is insufficiently capitalized or is not controlled through voting (or similar rights) should be consolidated.

      The conclusions reached in both of these Statements were used by the U.S. banking regulators in the recent stress tests on the major bank holding companies, and the FASB worked closely with banking regulators throughout the projects to communicate the anticipated changes to current guidance.

   c. In response to the global nature of accounting standards and the financial crisis, the FASB and IASB formed the Financial Crisis Advisory Group (FCAG), which is composed of 18 highly regarded individuals from countries throughout the world, for the purpose of providing the Boards with insight into the financial crisis using a forward-looking agenda. The FCAG meetings are
also being observed by different banking and regulatory agencies from countries throughout the world. Additionally, to facilitate a coordinated approach to significant joint projects, the FASB and IASB meet three times a year to discuss projects jointly.

d. The IASB plans to issue in July a final standard on international financial reporting standards (IFRS) for Small and Medium-Sized Entities (SME). That standard is designed to meet the financial reporting needs of private companies in the application of IFRS.

e. In response to the credit crisis, the FASB has issued:
   i. FSP FAS 157-4, Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly
   ii. FSP FAS 115-2, FAS 124-2, Recognition and Presentation of Other-Than-Temporary Impairments
   iii. FSP FAS 107-1 and APB 28-1, Interim Disclosures about Fair Value of Financial Instruments.

   Mr. Herz noted that investors have been interested in more granular and transparent disclosures, which is addressed through the significantly enhanced disclosure requirements in the three FSPs.

f. Mr. Herz noted that the Board voted to approve the FASB Accounting Standards Codification™ (Codification) as the single source of authoritative nongovernmental U.S. generally accepted accounting principles (GAAP). The Codification will be launched and available for use on July 1, 2009, and will be effective for interim and annual periods ending after September 15, 2009. In responding to a question, Mr. Herz noted that FASB Statement No. 168, The FASB Accounting Standards Codification™ and the Hierarchy of Generally Accepted Accounting Principles, which makes the Codification authoritative, will be the last FASB-issued Statement under the current numbering system. After July 1, new standards issued by the FASB will be in the form of “Accounting Standards Updates” and will follow a numbering system that is similar to the EITF consensuses. New standards will be composed of two items: the standard (similar to existing standards including the Basis for Conclusions) and an appendix containing Codification Update instructions.

g. Committee members raised questions about the Codification and Mr. Smith responded that:
   i. The Codification has many embedded links, which will facilitate more electronic use of the standards. A printed version will be available approximately three months after the Codification is launched.
   ii. The software revenue recognition questions and answers contained within AICPA technical practice aids were made authoritative for private companies (many of which were electing to follow the practice
Otherwise, the Codification does not have the intention to change U.S. GAAP. Companies are urged to contact the FASB if they identify differences in the application of the Codification versus current GAAP upon transition.

iii. The Codification is a web-based system and cannot be downloaded in its entirety. The FASB/FAF has the systems and information technology infrastructure to support a large number of simultaneous users of the Codification. The need for further capacity will be considered in the future.

iv. The Codification has a cross-reference tool to assist preparers and others in finding the location of current U.S. GAAP guidance within the Codification.

Report of the SEC

2. Ms. Minke-Girard provided an update about recent activities of the SEC:

a. The SEC staff will take a practical approach in reviewing and commenting on filings on the issue of references to the FASB’s Codification versus to “legacy” GAAP. For example, the SEC staff is not expecting to request that a company amend its previous SEC fillings to incorporate Codification references. The SEC staff also is suggesting that companies consider providing plain-English descriptions of accounting standards and concepts in their filings, rather than relying on numeric references to topics in the Codification.

b. The SEC staff is planning to recommend to the Commission that it issue an interpretation that explains that references in Commission rules and staff guidance to specific standards under U.S. GAAP should be interpreted to mean corresponding references in the FASB’s Codification. Furthermore, the SEC staff plans to undertake a project to identify all references in Commission rules and staff guidance to specific standards under U.S. GAAP and to make recommendations to the Commission to update or otherwise address those references.

c. The SEC staff issued Staff Accounting Bulletins 111 and 112, which conform SEC staff guidance with recently issued FASB guidance on (1) other than temporary impairments and (2) business combinations and noncontrolling interests, respectively. The SEC staff also is working to update Staff Accounting Bulletins on the accounting for oil- and gas-related entities. In April, the Commission issued final rules to adopt technical amendments to various rules, forms, and schedules to conform them to provisions in FASB Statement Nos. 141 (revised 2007), Business Combinations, and 160, Noncontrolling Interests in Consolidated Financial Statements.

(the “Proposed Rule”). The staff received letters from approximately 215 constituents, 35 of which were from investors/users. Based on the SEC staff’s initial analysis of comment letters, there appears to be general support for a single set of high-quality financial accounting and reporting standards, and many constituents view IFRS standards as a reasonable candidate for such a set of standards. However, the comment letters on the Proposed Rule also appear to reflect more variation in views as compared to the comment letters on the previous Concept Release.

e. The SEC created an Investor Advisory Committee, which is intended to give investors a greater voice in the SEC’s work.

Report of the PCAOB

3. Mr. Fletcher reported on recent PCAOB activities:

a. On April 21, 2009, the PCAOB issued a Staff Audit Practice Alert, Auditor Considerations Regarding Fair Value Measurements, Disclosures, and Other-Than-Temporary Impairments.

b. On April 14, 2009, the PCAOB issued Concept Release, Possible Revisions to the Standard on Audit Confirmations, for public comment until Friday, May 29, 2009. The staff received 21 comment letters; in general, respondents agreed with the direction of the PCAOB.

c. Last year the PCAOB proposed a new auditing standard, Engagement Quality Review, to replace the current interim requirements. The PCAOB received 38 comment letters on this proposal. The PCAOB considered the comments received, made significant changes to the standards in response, and issued a new proposal with comment letters due April 20, 2009. The PCAOB has received 30 comment letters on the new proposal.

d. In October 2008, the PCAOB proposed seven risk assessment standards. The comment period ended on February 18, 2009. The PCAOB received 33 comment letters. The staff is analyzing those comments and plans to make a recommendation to the PCAOB in the near future.

e. Nonpublic broker-dealers’ financial statements must be certified by a firm registered with the PCAOB effective for fiscal years ending after December 31, 2008. Currently, 1,951 firms from 86 countries have registered with the PCAOB. The PCAOB believes that as many as 1,500 additional firms could seek PCAOB registration in order to audit nonpublic broker-dealers.

f. The PCAOB’s Standing Advisory Group (SAG) met Thursday, April 2, 2009, to discuss going concern, audit confirmations, and the proposed auditing standard on engagement quality review. The PCAOB is soliciting nominations for the SAG for two-year terms that would begin in 2010. The deadline for submission is June 18, 2009.

g. Tom Ray, former Chief Auditor and Director of Professional Standards, left the PCAOB on March 6 to return to the private sector. Martin F. Baumann
has been named the new Chief Auditor of the Public Company Accounting Oversight Board.

Report of the PCFRC

4. Ms. O’Dell reported on recent PCFRC activities:
   a. The PCFRC had its first meeting with the FASB members in January 2009. The meeting was highly productive, and the PCFRC is enthusiastic about the direction the Board provided. Examples of issues the FASB brought to the attention of the PCFRC include:
      i. Providing more robust minutes,
      ii. Ensuring consideration of input from users of private company financial statements
      iii. Suggesting potential agenda items on the basis of private company financial reporting needs
      iv. Providing more specificity about the issues that affect private companies in writing future PCFRC comment letters on proposed FASB guidance.
   b. The PCFRC Chair participated in the FASB roundtable on loss contingencies and was a speaker at the AICPA’s IFRS conference. At the IFRS conference, participants expressed significant interest about how IFRS may affect private companies.

5. Committee members raised questions about the PCFRC, and Ms. O’Dell responded that:
   a. The PCFRC is very happy with the progress it has made in the past two years and looks forward to a continuously progressive relationship with the FASB.
   b. The FASB should be commended for its acknowledgement that it will more explicitly consider private company financial reporting needs in future decision-making meetings on its technical agenda projects.
   c. Focusing on the private company financial statement user view has helped the PCFRC further develop thoughtful responses to proposed FASB guidance. In addition, the PCFRC has spent more time reaching out for user views on specific FASB guidance.

Revenue Recognition in Contracts with Customers

6. Mr. Bement, FASB project manager, provided background about the revenue recognition model.
   a. The revenue recognition project is a joint project with the IASB. The objective of the project is to clarify the principles for recognizing revenue and to create a common standard that can be consistently applied to various transactions,
companies, and industries. In creating a single revenue recognition model, the FASB and IASB have been (and continue) seeking feedback on the model from advisory and other constituent groups.

b. The Boards issued a Discussion Paper in December 2008, which is available for comment through June 19, 2009. In general, constituents seem to support a single revenue recognition model in contracts with customers and cautiously accept the proposed model. However, responses received so far are asking for modifications or clarifications.

c. In the past few months, the Boards have been deliberating issues that were not in the Discussion Paper, including the measurement of rights in a contract. Also, in the coming months, the Boards will be considering other issues including renewal and cancellation options in a contract, collectibility, gross versus net presentation of revenue, gross versus net presentation of the rights and obligations in a contract, and the combination and segmentation of contracts.

d. The EITF has been considering revenue-related issues, including EITF Issues No. 08-1, "Revenue Arrangements with Multiple Deliverables," No. 09-3, "Applicability of AICPA Statement of Position 97-2 to Certain Arrangements That Include Software Elements," and No. 08-9, "Milestone Method of Revenue Recognition."

7. Mr. Bement asked members for their input. Members provided comments about the time value of money in measuring contract rights, the application of the model to specific transactions or industries, contract acquisition costs, and the measurement of contracts and selling prices. In general, committee members supported one model for recognizing revenue in contracts with customers and thought that the proposal model was an appropriate model to fulfill this purpose. In considering the proposed model, a committee member also noted that the notion of control seems overly legalistic and suggested that the staff consider forming criteria to determine when control is transferred.

**Measurement of Contract Rights: Time Value of Money**

8. Committee members spent significant time discussing the time value of money as a component of the measurement of rights. Mr. Bement introduced a situation for discussion in which two companies have contracts to deliver identical goods and services. One company requires a customer to prepay, and the other company allows the customer to pay at a time significantly after performance. In that situation, the Boards decided that the companies have different transaction prices, which should be reflected when significant.

9. A committee member asked that the FASB remain careful in how it evaluates significance and suggested a practical cutoff of a year to accommodate many normal sales transactions. Other committee members also expressed concerns about the time value of money:
a. In general, committee members were skeptical about decreasing the amount of revenue that can be recognized because of a delay in the date a customer’s payment is received.

b. Different recognition and measurement requirements, including taking into consideration the effect of time value of money, increase the burden on preparers to reconcile between tax and financial accounting.

c. The flexibility created by not having a bright line in determining when the time value of money is significant creates incomparability among financial statements.

10. Mr. Herz responded that the Board rejected a bright-line time frame or specific interest rate hurdle to determine when the time value of money is significant because

   a. Significance depends on where in the world the entity operates and the circumstances that affect that specific entity.

   b. Bright lines create false comparability because an entity can change the accounting it uses depending on if the company structures a transaction below or above a very specific threshold.

11. A committee member agreed with rejecting bright-line hurdles because low inflation may be material in the long term and high inflation may be very material in the short term. Another committee member noted that the time value of money often will not be recognized in the net contract position of an entity under current accounting practices. That committee member also complemented the FASB for the principles-based mentality it has retained in this project. Mr. Smith explained that a tradeoff exists between rules that are overly complicated and principles that raise questions as to the comparability of financial statements. Mr. Smith stated the FASB strives to perfect a balance between these two issues.

The Application of the Model to Specific Transactions or Industries

12. A committee member noted that if examples for specific industries (specifically the pharmaceuticals and biotechnologies industries) are part of the final standard, the staff must be very careful to ensure that it faithfully represents contracts from that industry.

13. A committee member asked how to account for situations in which a company provides a service of giving the customer “peace of mind”; for example, when a servicer promises to provide the service of standing ready to fix, repair, or otherwise perform work on a good owned by the customer, either at the discretion of the customer or the servicer. Mr. Linsmeier noted that it appears that the company has a performance obligation to provide maintenance, service, etc. Mr. Bement explained that the model would have an entity first identify what asset it has promised and then determine when it transfers control of that asset to the customer.

14. Another committee member asked how warranties would be accounted for under the proposed model. Mr. Bement explained that the model does not distinguish between standard and extended warranties. However, Mr. Bement explained that in
light of comments received, the staff thinks a difference may exist between standard warranties and extended warranties. For example, there may be uncertainty about past performance in which a product is not what it was promised to be (e.g., standard warranty) or there may be uncertainty about a promise to provide future performance (e.g., an extended warranty).

15. Another committee member asked whether and how the revenue model would be applied by financial services companies. Mr. Bement explained that the staff plans to reach out to financial service firms in the near future and will further consider the potential application of the model to financial service transactions.

16. In responding to a question about how the proposed model will affect take-or-pay contracts, Mr. Smith noted that the company will recognize revenue when it satisfies its performance obligation.

**Contract Acquisition Costs**

17. A committee member noted that instead of expensing contract acquisition costs, the Board should consider allowing entities to record an intangible asset. Mr. Linsmeier noted that expensing acquisition costs is a question of whether obtaining a customer is a performance obligation and that, if so, revenue should be recognized at contract inception, possibly only enough to offset the actual costs incurred.

18. Another committee member agreed with the proposed models of expensing acquisition costs.

**Measurement of Contracts and Selling Prices**

19. A committee member asked whether the Board has considered ignoring onerous contracts. Mr. Linsmeier responded that onerous contracts are a one-sided way of measuring contracts. A few Board members agreed with a committee member's observation that onerous contract accounting is a form of conservatism.

20. Mr. Smith introduced the issue of multiple-element contracts and whether to require a company to estimate the standalone selling price of a good or service that does not have an otherwise observable independent price. Mr. Smith noted that this issue is being considered by the EITF and in the proposed revenue recognition model, and he asked for SBAC members' feedback.

   a. A committee member noted that conceptually he agrees with work the EITF has done and the direction of the proposed model.
   
   b. Another committee member noted that he sees difficulty in valuing something that is not sold separately.
   
   c. Mr. Linsmeier asked whether the proper checks and balances exist in practice to ensure companies do not manipulate the timing of revenue recognition. Mr. Bement explained that this issue is important to the proposed model, as it determines the segmentation of the margin in a contract.
   
   d. Mr. Linsmeier noted that as opposed to current accounting, under the proposed model, if an entity sells a product with a warranty, an entity
would recognize revenue both upon delivery of the product and over the course of the warranty. The entity would recognize the costs of the product and the costs of the warranty as incurred. Mr. Bement noted that the model proposes that different margins are essentially allocated and further recognized upon the satisfaction of individual performance obligations. Mr. Bement noted that this is particularly problematic in the construction industry.

e. A committee member responded that it appears revenue will be recognized earlier in the proposed model than in current guidance in situations, such as biotech arrangements, in which an entity receives consideration if it achieves a specific milestone.

21. Mr. Smith noted that the Boards have agreed that when the amount of consideration to be received by the supplier is uncertain (i.e., variable), the amount allocated to performance obligations would be the entity’s probability-weighted estimate of total consideration. Furthermore, the Boards have agreed that revenue recognition should be constrained only if the consideration amount cannot be reliably estimated. Mr. Smith asked SBAC members for their comments on this issue. A committee member responded that the issue raised may be easier to handle when an entity has a group of homogeneous transactions or a good history of similar transactions.

Current and Future Financial Reporting Issues

22. Mr. Smith asked the committee members whether there are any current or future financial reporting issues that the Board should be aware of or should consider adding to its technical project agenda.

23. Committee members responded with a number of different areas for the Board’s consideration, including:

   a. The reversibility of other-than-temporary impairments that result from credit losses. A committee member suggested that this topic should be added to the Board’s agenda before it becomes a major concern. Ms. Seidman asked whether the reversibility issue relates equally to an impairment write-down as a result of a credit loss and an impairment write-down as a result of an entity’s inability to assert that it can sell the security. Ms. Seidman stated that she would be opposed to reversing other-than-temporary impairments that are a result of cash flows becoming uncollectible.

   b. Unfunded contingent liabilities associated with multi-employer pension plans. Several committee members stated that as a result of both the economic crisis and the Bernie Madoff scandal, multi-employer pension plans across the nation are becoming underfunded, and entities are scrambling to find ways to fund these plans. Furthermore, it is uncertain how to appropriately calculate the contingent liability of pension plans and determine what amount each member of the multi-employer plan must contribute because it is currently a convoluted and complicated process. Mr. Herz agreed and stated that calculating the contingent liability associated with multi-employer plans is not an exact science and that the lack of timely information in this area further
complicates this. Ms. Seidman asked whether more disclosures would help to resolve the issues about multi-employer pension plans, as those plans could be included within the FASB’s project on disclosures of certain loss contingencies. A committee member agreed that additional disclosure would be helpful because there is not necessarily a correct way to calculate the contingent liability.

c. Revisiting the current goodwill impairment model. A committee member suggested that the Board evaluate the cost versus benefit of the current goodwill impairment model. He supported that evaluation because (a) the valuation process for goodwill is expensive and (b) it is unclear whether the current goodwill accounting produces better information than what was produced under the previous amortization model. Whether a company argues to amortize or to impair goodwill hinges on whether the company would like to maximize or minimize its amortization expense. Mr. Herz responded that the previous Board considered the cost versus benefit of the current goodwill impairment model. He questioned whether the trade-off issue is experienced only by nonpublic entities or if it was applicable to public entities as well. The committee member responded that it is an issue for both types of entities because amortization expense affects net income for public entities and it also affects the manner in which analysts value the company (i.e., consider goodwill decreases as one-time charges that tend to be ignored or as normalized charges that are a part of a company’s normal operations).

d. The valuation and recording of purchased items (e.g., inventory) at a fair value less selling costs in an acquisition of a business. A committee member observed that the acquisition value tends to be a higher value than the original cost to the acquiree. As a result, net income is distorted because cost of goods sold is higher than it should be and comparability between companies is destroyed until the old, purchased inventory is sold. That is also an issue with items, such as loan covenants, which are sometimes dependent on net income. Mr. Golden responded that he would inquire as to how the Valuation Resource Group dealt with this issue.

e. Possible write-off of operating contracts. A committee member stated that his company purchases television programming, but because of factors including the economy and lower television ratings, the value of current contracts that are negotiated are less than the operating contracts recorded in the past. As a result, it is unclear whether a company is allowed to write down these types of operating contracts to account for the decline in value. The committee member stated that this issue is applicable to any industry where companies agree to purchase particular inventory at set prices in the future but because of outside factors, the value of the items decline and the purchasing company is forced to sell these items at a loss.

f. The meaning of significant versus the meaning of material. A committee member suggested that those meanings needed clarification as the FASB and the IASB work toward convergence. The term significant has statistical meaning, while the term material pertains to whether an investor would make
a decision on the basis of the information. That committee member stated that it would be convenient to have a standard definition of terms that are frequently used by the FASB to facilitate users’ understanding of accounting guidance.

g. Reversals for impairments. A committee member stated it may be valuable, for the sake of neutrality and convergence, for the FASB to consider adopting IASB guidance on reversibility of impairments. Mr. Herz responded that the IASB does not have a “cushion” for undiscounted cash flows in determining impairments, which results in companies reaching the “trigger” to recognize impairments more quickly than companies using the FASB’s impairment guidance.

h. Accounting and disclosure of allowances for loan losses. A committee member stated that the accounting and disclosure of allowances for loan losses should be added to the Board’s agenda. Mr. Smith responded that the FASB is currently working on the disclosure of allowances for loan losses within its loan loss disclosures project and an exposure draft would be issued in the coming weeks. Mr. Smith also stated that accounting for the allowance for loan losses is within the scope of the joint financial instruments project.

**FIN 48—Applicability for Private Companies**

24. Mr. Glotzer began the discussion by providing brief information about the project and asking for input on the questions raised in the Notice for Recipients included in the proposed FSP.

25. A committee member suggested that another example should be added after paragraph 28 of the proposed FSP that illustrates a situation in which the reporting entity of a consolidated group is a taxable entity with a nontaxable subsidiary instead of only having an example that illustrates a nontaxable entity reporting with a taxable subsidiary. Mr. Glotzer responded that the example was intended to clarify that the status of the reporting entity is not what governs whether the consolidated financial statements are included in the scope of Interpretation 48 but instead the decision is dependent on whether there are any members of the consolidated group that are subject to Interpretation 48.

26. Another committee member stated that paragraph 8(c) of the proposed FSP on Interpretation 48 should be moved to become 8(a) because it would make it clearer that if income taxes are attributed to the owners and not the entity, Interpretation 48 does not apply. The committee member stated that if taxes are attributed to the owners, there is no further assessment of a tax uncertainty for that entity. Mr. Glotzer stated that if all the income taxes in all jurisdictions were attributable to the owners, then the entity’s assessment of its tax uncertainty may be complete; however, if the entity issues consolidated or combined financial statements, it must also consider whether any entity within the reporting group is subject to Interpretation 48.
Financial Statement Presentation

27. Mr. Cappiello opened the session with a synopsis of the recent progress made on the Financial Statement Presentation project. More than 200 comment letters have been received, and the staff is currently in the process of summarizing and analyzing the responses. He stated that the staff is focusing on three main topics from the presentation model: (a) disaggregation by function and nature within the statement of comprehensive income, (b) the direct method cash flow statement, and (c) the reconciliation schedule.

28. Much of the session was spent discussing both the indirect method cash flow statement, which most companies use today, and the direct method cash flow statement, which the recent Discussion Paper proposed that companies adopt. Committee members also commented on the proposed disaggregation requirements, the reconciliation schedule, whether the current presentation model is sufficient, whether the proposed presentation model would be useful in a private company environment, and other suggestions about the project conduct.

Direct Method Cash Flow Statement

29. Many committee members raised concerns about the operationality, costs, and benefits of requiring a direct method cash flow statement, as well as the benefits of the indirect cash flow statement:

   a. Many preparers would find it challenging to create a direct method cash flow statement because many larger companies may have standalone systems that run on different types of software that do not have the capability to capture the nature of cash flows in order to create a consolidated direct method cash flow statement. As a result, most companies would need to retool their systems, which would be an expensive process.

   b. Users benefit a lot from an indirect method cash flow statement because this statement provides a summary of working capital movements. These working capital movements are helpful for users in discovering why the cash balance is not where it was anticipated to be. Furthermore, the indirect method cash flow statement provides better information on what the company’s “burn rate” is, which is defined as net income less depreciation, amortization, stock-based compensation, etc. The direct method cash flow statement does not provide any of this information.

   c. The indirect method cash flow statement will allow for better fraud investigation, because it will be possible to see how the cash balance reconciles to the net income number provided.

30. Mr. Smith added that many users think the direct method cash flow statement does not provide better information than the indirect method cash flow statement. Mr. Linsmeier disagreed, noting that academic research states that a direct method cash flow statement created using the indirect-direct method produces significantly less accurate numbers (a) for the operating, financing, and investing subtotals and (b) within the operating section, than those direct method cash flow statements
created using the direct-direct method. Furthermore, a direct method cash flow statement indicates which operating cash flows are more persistent, which helps to more accurately predict future cash flows. As a result, a “direct-direct” cash flow statement can be used to back into the accrual numbers needed for solid fraud investigation work.

**Disaggregation Requirements**

31. A committee member stated that the additional disaggregation required in the proposed financial statement presentation may push many private companies to adopt the IASB’s “Small and Medium-sized Entities” (SME) project’s requirements because private companies do not want to disclose very much information. There is a lot of competition among private entities, and any additional disclosure requirements will serve as a disadvantage. For instance, some private companies provide their financial statements to customers. If more information about the costs for products is given to customers via disaggregation in the financial statements, customers will demand that the seller provide a lower price. As a result, the Boards should consider more aggregation of information to prevent such scenarios. The committee member added that the Boards must have a balance in what they are requiring businesses to present in the financial statements and must be cognizant of management’s perspective as well. The committee member further supported his argument by drawing an analogy to the reason private companies are not required to present segment information—because it would reveal too much about the company.

32. In regards to additional disaggregation within the financial statements, another committee member stated that managerial accountants would welcome the additional information because it will help to better obtain the contribution margin. Furthermore, the additional disaggregation would help users create more predictive models.

**Reconciliation Schedule**

33. A committee member stated that she did not think the reconciliation schedule would be useful for users because when her company provides the cash flow statement to users, they do not ask for the type of information found within the reconciliation schedule. Mr. Cappiello added that many respondents during the comment letter period called for different types of reconciliations, such as a balance sheet to balance sheet reconciliation. Respondents also stated that the complexity and detail of the proposed reconciliation schedule are not needed and that the model may want to focus on only a few key line items and not a reconciliation of every line item shown in the current illustration. Mr. Linsmeier stated that several constituents have stated that it may be redundant to provide both the direct method cash flow statement and the reconciliation schedule because the reconciliation schedule already contains the information from the direct method cash flow statement.

**The Current Presentation Model**

34. Several committee members stated that there is nothing wrong with the current financial statement presentation requirements and no reason to change them. A
committee member stated that although the current presentation model is flawed in many ways, users have become accustomed to the presentation model and can get the information they need from the existing model. Committee members noted that many of the ideas within the Discussion Paper are conceptually sound but are not very practical. Another committee member commented that it is unclear whether users are going to benefit from the new presentation model to justify the costs—both in actual dollars spent and the proprietary information given up. Ms. Seidman disagreed, however, stating that the proposed presentation model will provide coherence between the individual financial statements within a period and the same financial statement from period to period (e.g., balance sheet to balance sheet reconciliation). Another committee member stated, and Mr. Herz agreed, that there is a lot to fix within financial statements today, because the redundancy within the notes and MD&A needs to be eliminated.

35. Mr. Linsmeier stated that management often manages its business by nature internally. A committee member agreed by stating that management does not use today's financial statement presentation format to manage its business because it does not provide the necessary level of detail to do so effectively.

36. A committee member stated that the concept of splitting account balances into the operating, investing, and financing sections will provide beneficial information. Another committee member representing financial institutions stated that he is more worried about forecasting liquidity needs than seeing historically what the cash flows were.

The Proposed Presentation Model in a Private Company Context

37. A committee member stated the SME project being undertaken by the IASB has already created a set of financial statements that includes an indirect method cash flow statement. As a result, if the Boards issue a standard inconsistent with the IASB's SME project, there is a possibility of criticism of standard setters, which will be a detriment to their credibility. Mr. Linsmeier stated that the IASB might need to consider whether to amend the requirements of the SME standard on the basis of their conclusions in the Financial Statement Presentation project. An FASB staff member observed that any amendments to the SME standard would be done on a periodic basis (included in a two-year cycle) rather than on a continuous basis. As a result, it may be problematic should the two Boards make separate financial statement presentation requirements that are contradictory within a short period of time. Mr. Smith responded that the SME standard would be optional for private companies and questioned whether it is important for private companies to have a consistent financial statement presentation as public companies in the U.S. and abroad.

38. A committee member reminded the group that the purpose of financial statements is different for private company users than for public company users. In other words, users of public company financial statements ultimately want to project what the stock price will be, while users of private company financial statements want to see the fiscal strength of the company. Ms. Seidman reiterated that the Boards have not
made a decision about whether the proposed presentation model would be applied to private companies.

39. Another committee member stated that this project is aimed solely toward equity analysts and their quest for useful information in the financial statements, which is not applicable to private companies and their users. That committee member suggested that the Boards continue to focus on public users and their needs for this project. Once the Boards have created the presentation model for public companies, the Boards should then analyze whether or not there is any demand for change in the presentation model for private companies. Mr. Herz added that the Boards should also determine whether users are willing to handle a difference in presentation between public and private companies.

Other Suggestions

40. Committee members also suggested that:

   a. The Boards determine whether much of the proposed presentation information could be reported within the notes as supplemental information, rather than on the face of the statements.

   b. Educational efforts for users—especially regulatory users—are imperative because many users may not know how to best find the information they are looking for within the proposed presentation model.

   c. “Best practices” will need to be developed for particular industries within the presentation principles provided in the Financial Statement Presentation project.

Adjournment

41. Mr. Smith thanked committee members for their preparation for and participation in the meeting and adjourned the meeting at 3:00 p.m.