



EXPOSURE DRAFT

Proposed Accounting Standards Update

Issued: August 7, 2013

Comments Due: September 20, 2013

Definition of a Public Business Entity

An Amendment to the Master Glossary

This Exposure Draft of a proposed Accounting Standards Update is issued by the Board for public comment. Comments can be provided using the electronic feedback form available on the FASB website. Written comments should be addressed to:

Technical Director

File Reference No. 2013-310

Financial Accounting Standards Board
of the Financial Accounting Foundation

The *FASB Accounting Standards Codification*[®] is the source of authoritative generally accepted accounting principles (GAAP) recognized by the FASB to be applied by nongovernmental entities. An Accounting Standards Update is not authoritative; rather, it is a document that communicates how the Accounting Standards Codification is being amended. It also provides other information to help a user of GAAP understand how and why GAAP is changing and when the changes will be effective.

Notice to Recipients of This Exposure Draft of a Proposed Accounting Standards Update

The Board invites comments on all matters in this Exposure Draft and is requesting comments by September 20, 2013. Interested parties may submit comments in one of three ways:

- Using the electronic feedback form available on the FASB website at [Exposure Documents Open for Comment](#)
- Emailing a written letter to director@fasb.org, File Reference No. 2013-310
- Sending written comments to “Technical Director, File Reference No. 2013-310, FASB, 401 Merritt 7, PO Box 5116, Norwalk, CT 06856-5116.”

Do not send responses by fax.

All comments received are part of the FASB’s public file. The FASB will make all comments publicly available by posting them to the online public reference room portion of its website.

An electronic copy of this Exposure Draft is available on the FASB’s website.

Copyright © 2013 by Financial Accounting Foundation. All rights reserved. Permission is granted to make copies of this work provided that such copies are for personal or intraorganizational use only and are not sold or disseminated and provided further that each copy bears the following credit line: “Copyright © 2013 by Financial Accounting Foundation. All rights reserved. Used by permission.”

Proposed Accounting Standards Update
Definition of a Public Business Entity
An Amendment to the Master Glossary

August 7, 2013

Comment Deadline: September 20, 2013

CONTENTS

	Page Numbers
Summary and Questions for Respondents.....	1–5
Amendments to the <i>FASB Accounting Standards Codification</i> ®	7–8
Background Information and Basis for Conclusions	9–19
Amendments to the XBRL Taxonomy	20

Summary and Questions for Respondents

Why Is the FASB Issuing This Proposed Accounting Standards Update (Update)?

The Board has received inquiries from stakeholders about which entities will be within the scope of the draft *Private Company Decision-Making Framework: A Guide for Evaluating Financial Accounting and Reporting for Private Companies* (guide) once it is finalized and about the inconsistency and complexity of having multiple definitions of a nonpublic entity and public entity within U.S. generally accepted accounting principles (GAAP). Specifically, stakeholders asked that the Board clarify which nonpublic entities potentially would qualify for alternative accounting and reporting guidance. This proposed Update would help address those issues by proposing a definition of a *public business entity*.

The primary purposes of this proposed Update are to:

- a. Amend the Master Glossary of the *FASB Accounting Standards Codification*[®] to include one definition of public business entity for use in U.S. GAAP. The proposed amendments would not affect existing requirements. That definition would be used by the Board, the Private Company Council (PCC), and the Emerging Issues Task Force (EITF) in specifying the scope of future accounting and reporting guidance.
- b. Identify the types of business entities that would be excluded from the scope of the guide. Other types of entities that would be excluded from the scope of the guide are not-for-profit entities (NFPs) and employee benefit plans within the scope of Topics 960 through 965 on plan accounting. Business entities that are within the scope of the guide are those for which the Board and the PCC would consider potential accounting and reporting alternatives within U.S. GAAP. However, even if an entity is within the scope of the guide, that entity may not necessarily be eligible to apply all financial accounting and reporting alternatives within U.S. GAAP that are made available to private companies.

The Board also will evaluate whether a particular accounting or reporting alternative that is permitted to be applied by a business entity within the scope of the guide should be extended to a public business entity, an NFP, or an employee benefit plan within the scope of Topics 960 through 965 on plan accounting.

Who Would Be Affected by the Amendments in This Proposed Update?

The definition of a public business entity would be used in determining the scope of new accounting and reporting guidance and would identify whether the guidance would or would not apply to public business entities. The proposed definition would exclude an NFP or an employee benefit plan within the scope of Topics 960 through 965 on plan accounting and would not affect existing requirements. Business entities that are within the scope of the guide are those for which the Board and the PCC would consider potential accounting and reporting alternatives within U.S. GAAP.

What Are the Main Provisions?

The proposed amendments would define a public business entity as a business entity meeting any one of the following criteria:

1. It is required by the U.S. Securities and Exchange Commission (SEC) to file or furnish financial statements, or does file or furnish financial statements, with the SEC (including other entities whose financial statements or financial information are required to be or are included in a filing).
2. It is required by the Securities Exchange Act of 1934, as amended, or rules or regulations promulgated under the Act, to file or furnish financial statements with a regulatory agency.
3. It is required to file or furnish financial statements with a regulatory agency in preparation for the sale of securities or for purposes of issuing securities.
4. It has (or is a conduit bond obligor for) unrestricted securities that are traded or can be traded on an exchange or an over-the-counter market.
5. Its securities are unrestricted, and it is required to provide U.S. GAAP financial statements to be made publicly available on a periodic basis pursuant to a legal or regulatory requirement.

This excludes an NFP or an employee benefit plan within the scope of Topics 960 through 965 on plan accounting.

How Would the Main Provisions Differ from Current U.S. Generally Accepted Accounting Principles (GAAP) and Why Would They Be an Improvement?

The Accounting Standards Codification includes multiple definitions of the terms *nonpublic entity* and *public entity*. The amendments in this proposed Update

would improve U.S. GAAP by providing a single definition of a public business entity for use in future accounting and reporting guidance. The proposed amendments would not affect existing requirements. The Board could consider whether to undertake a second phase of the project at a later stage to examine whether to amend current U.S. GAAP with a new definition resulting from this proposed Update.

The proposed definition of a public business entity would differ from some of the existing definitions of a public entity in the Accounting Standards Codification. The proposed amendments would specify that:

1. An entity that is required by the SEC to file or furnish financial statements with the SEC, or does file or furnish financial statements with the SEC, is considered a public business entity. Some of the existing definitions of a public entity in the Accounting Standards Codification do not include this criterion to define a public entity.
2. A consolidated subsidiary of a public company would not be considered a public business entity for purposes of its standalone financial statements other than those included in an SEC filing by its parent or by other registrants. Some of the existing definitions of a public entity in the Accounting Standards Codification consider a consolidated subsidiary of a public company to be public.
3. A business entity that has securities that are unrestricted and that is required to provide U.S. GAAP financial statements to be made publicly available on a periodic basis pursuant to a legal or regulatory requirement would be considered a public business entity. The existing definitions of a public entity in the Accounting Standards Codification do not include this criterion and would not consider an entity to be public unless it meets one of the other criteria included in the definition (for example, if it has debt or equity securities that trade either on a stock exchange or an over-the-counter market).

Generally, most NFPs have received the same accounting and reporting alternatives within U.S. GAAP that have been available to nonpublic business enterprises. Distinctions about which NFPs would receive accounting and reporting alternatives within U.S. GAAP typically have been made on the basis of whether an NFP has public debt securities, including conduit debt. The proposed amendments would exclude all NFPs from the definition of a public business entity so that a public versus nonpublic distinction would no longer be made between NFPs in future standard setting. Instead, the Board would consider factors such as user needs and NFP resources, on a standard-by-standard basis, when determining whether all, none, or only some NFPs will be eligible to apply accounting and reporting alternatives within U.S. GAAP for private companies.

When Would the Amendments Be Effective?

The Board would not finalize the amendments in this proposed Update until the new term *public business entity* is used in an amendment to a Topic in the Accounting Standards Codification. Therefore, the effective date of the amendments in this proposed Update would be established concurrently with the first Update that uses the definition of a public business entity.

How Do the Proposed Provisions Compare with International Financial Reporting Standards (IFRS)?

The amendments in this proposed Update are not expected to create any new differences between U.S. GAAP and IFRS. A key difference between the applicability of IFRS and U.S. GAAP is that IFRS provides for accounting and reporting alternatives for entities that do not have public accountability through the use of a separate set of standards for small and medium-sized entities (SMEs).

The term *small and medium-sized entities* as used by the International Accounting Standards Board (IASB) is defined as entities that (1) do not have public accountability and (2) publish general purpose financial statements for external users. An entity has public accountability if:

1. It files, or it is in the process of filing, its financial statements with a securities commission or other regulatory organization for the purpose of issuing any class of instruments in a public market, or
2. It holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses. This is typically the case for banks, credit unions, insurance companies, securities brokers/dealers, mutual funds, and investment banks.

In contrast, the FASB and the PCC aim to achieve an appropriate cost-benefit balance by providing accounting and reporting alternatives to entities that are within the scope of the guide (which is not based on the notion of public accountability). In addition, accounting and reporting alternatives are provided within a single set of U.S. GAAP guidance.

Questions for Respondents

The Board invites individuals and organizations to comment on all matters in this proposed Update, particularly on the issues and questions below. Comments are requested from those who agree with the proposed guidance as well as from those who do not agree. Comments are most helpful if they identify and clearly explain the issue or question to which they relate. Those who disagree with the

proposed guidance are asked to describe their suggested alternatives, supported by specific reasoning.

Question 1: Please describe the entity or individual responding to this request. For example:

- a. Please indicate whether you primarily are a preparer, user, or public accountant. If other, please specify.
- b. If you are a preparer of financial statements, please indicate whether your entity today is considered privately held or publicly held and describe your primary business and its size (in terms of annual revenue, the number of employees, or other relevant metric).
- c. If you are a public accountant, please describe the size of your firm (in terms of number of partners or other relevant metric) and indicate whether your practice focuses primarily on public entities, private entities, or both.
- d. If you are a user of financial statements, please indicate in what capacity (for example, lender, investor, analyst, or rating agency) and whether you primarily use financial statements of private entities or those of both private entities and public entities.

Question 2: Do you agree with the definition of a public business entity included in this proposed Update? Please explain why.

Question 3: Do you agree that a business entity that has securities that are unrestricted and that is required to provide U.S. GAAP financial statements to be made publicly available on a periodic basis pursuant to a legal or regulatory requirement should be considered a public business entity? Please explain why. Can you identify a situation in which an entity would meet this criterion but would not meet any of the other criteria identified in the definition of a public business entity? In addition to what is discussed in paragraph BC18 of this proposed Update, do you think further clarification is needed to determine what an unrestricted security is?

Question 4: Do you agree that no public or nonpublic distinction should be made between NFPs for financial reporting purposes? Instead, the Board would consider whether all, none, or only some NFPs should be permitted to apply accounting and reporting alternatives within U.S. GAAP. Please explain why.

Question 5: Should the Board consider whether to undertake a second phase of the project at a later stage to examine whether to amend existing U.S. GAAP with a new definition resulting from this proposed Update? In that second phase of the project, the Board would consider whether to (a) preserve the original scope of guidance in the Accounting Standards Codification or (b) change the scope of guidance in the Accounting Standards Codification to align with the new definition. Please explain why.

Amendments to the *FASB Accounting Standards Codification*[®]

Summary of Proposed Amendments to the Accounting Standards Codification

Introduction

1. The Accounting Standards Codification is amended as described in paragraph 2. In some cases, to put the change in context, not only are the amended paragraphs shown but also the preceding and following paragraphs. Terms from the Master Glossary are in **bold** type. Added text is underlined, and deleted text is ~~struck-out~~.

Amendment to Master Glossary

2. Add the new Master Glossary term *Public Business Entity* as follows:

Public Business Entity

A business entity meeting any one of the following criteria would be considered public:

- a. It is required by the U.S. Securities and Exchange Commission (SEC) to file or furnish financial statements, or does file or furnish financial statements, with the SEC (including other entities whose financial statements or financial information are required to be or are included in a filing).
- b. It is required by the Securities Exchange Act of 1934, as amended, or rules or regulations promulgated under the Act, to file or furnish financial statements with a regulatory agency.
- c. It is required to file or furnish financial statements with a regulatory agency in preparation for the sale of securities or for purposes of issuing securities.
- d. It has (or is a conduit bond obligor for) unrestricted securities that are traded or can be traded on an exchange or an over-the-counter market.
- e. Its securities are unrestricted, and it is required to provide U.S. GAAP financial statements to be made publicly available on a periodic basis pursuant to a legal or regulatory requirement.

This excludes a not-for-profit entity or an employee benefit plan within the scope of Topics 960 through 965 on plan accounting.

The amendments in this proposed Update were approved for publication by the unanimous vote of the six members of the Financial Accounting Standards Board:

Russell G. Golden, *Chairman*
Daryl E. Buck
Thomas J. Linsmeier
R. Harold Schroeder
Marc A. Siegel
Lawrence W. Smith

Background Information and Basis for Conclusions

Introduction

BC1. The following summarizes the Board's considerations in reaching the conclusions in this proposed Update. It includes reasons for accepting certain approaches and rejecting others. Individual Board members gave greater weight to some factors than to others.

BC2. The primary purposes of this proposed Update are to:

- a. Amend the Master Glossary of the Accounting Standards Codification to include one definition of *public business entity* for use in U.S. GAAP. The proposed amendments would not affect existing requirements. That definition would be used by the Board, the PCC, and the EITF in specifying the scope of future accounting and reporting guidance.
- b. Identify the types of business entities that would be excluded from the scope of the draft *Private Company Decision-Making Framework: A Guide for Evaluating Financial Accounting and Reporting for Private Companies* (guide). The other types of entities that would be excluded from the scope of the guide are NFPs and employee benefit plans within the scope of Topics 960 and 965 on plan accounting. Business entities that are within the scope of the guide are those for which the Board and the PCC would consider potential accounting and reporting alternatives within U.S. GAAP. However, even if an entity is within the scope of the guide, that entity may not necessarily be eligible to apply all financial accounting and reporting alternatives within U.S. GAAP that are made available to private companies.

BC3. The Board also will evaluate whether a particular accounting or reporting alternative that is permitted to be applied by a business entity within the scope of the guide also should be extended to a public business entity, an NFP, or an employee benefit plan within the scope of Topics 960 through 965 on plan accounting. However, the Board acknowledges that decisions about whether an entity may apply permitted differences within U.S. GAAP may ultimately be determined by regulators (for example, the SEC and financial institution regulators), lenders and other creditors, or other financial statement users that may not accept financial statements that reflect accounting or reporting alternatives for private companies.

BC4. The proposed definition would exclude an NFP or an employee benefit plan within the scope of Topics 960 through 965 on plan accounting.

Background Information

BC5. The Board has received inquiries from stakeholders about which entities will be within the scope of the draft *Private Company Decision-Making Framework: A Guide for Evaluating Financial Accounting and Reporting for Private Companies* (guide) once it is finalized and about the inconsistency and complexity of having multiple definitions of a nonpublic entity and public entity within U.S. GAAP. Those different definitions of the terms nonpublic entity and public entity were established to address the scope of an individual standard, differences in accounting or disclosure requirements, and deferred effective dates. Specifically, stakeholders asked that the Board clarify which nonpublic entities potentially would qualify for alternative accounting and reporting guidance.

BC6. The objectives of the project include identifying the scope of entities that would be considered in future deliberations about potential accounting and reporting alternatives within U.S. GAAP, simplifying the definition of a nonpublic entity, and addressing known practice issues.

BC7. On July 31, 2012, after consultation with the Board, the staff issued an Invitation to Comment on a paper that outlined an approach for deciding whether and when to modify U.S. GAAP for private companies. The paper, *Private Company Decision-Making Framework: A Framework for Evaluating Financial Accounting and Reporting Guidance for Private Companies*, contained initial FASB staff recommendations of criteria to determine whether and in what circumstances it is appropriate to adjust financial reporting requirements for private companies following U.S. GAAP. The Board's tentative decisions reached to date about the definition of a private company and organizations in the scope of the guide were included in an appendix to the Invitation to Comment.

BC8. On April 15, 2013, the Board and the PCC issued an Invitation to Comment, *Private Company Decision-Making Framework: A Guide for Evaluating Financial Accounting and Reporting for Private Companies*. That Invitation to Comment includes the Board's tentative decisions about the types of business entities that would not be included in the scope of the guide.

BC9. The Board considered the feedback received by stakeholders on the 2012 and 2013 Invitations to Comment when reaching the conclusions in this proposed Update.

BC10. The following sections of the basis for conclusions in this proposed Update include the factors that were considered by the Board in defining a public business entity.

Entities That File or Furnish Financial Statements with the SEC and Entities That Issue Securities or Have Securities That Trade

BC11. Under all of the definitions of a nonpublic entity and public entity in the Accounting Standards Codification, entities that file financial statements with a regulatory agency in preparation for the sale of securities or for the purpose of issuing securities are defined as public companies. The financial statement users of entities that issue securities that trade in a public market generally lack direct access to management to obtain material financial information, and it is common for there to be a large number of financial statement users that have broader, more diverse needs and that use financial information for different reasons than typical users of private company financial statements. The six significant differential factors between public companies and private companies described in the guide were developed primarily on the basis of entities that access the public capital markets by issuing securities that are publicly traded. Therefore, when assessing those entities and their relationship to the six significant differential factors, the Board concluded that those entities should be considered public business entities.

BC12. The SEC requires certain financial statements to be filed or furnished in order to regulate the capital markets for securities and to protect investors in the public capital markets. For similar reasons as indicated in paragraph BC11, the Board reached a conclusion that an entity that is required by the SEC to file or furnish financial statements, or does file or furnish financial statements with the SEC, should be considered a public business entity (for example, broker-dealers). This also includes an entity's financial statements or financial information that is required to be or is included in a filing with the SEC (for example, Regulation S-X, Rule 3-09, *Separate Financial Statements of Subsidiaries Not Consolidated and 50 Percent or Less Owned Persons*). The Board decided that in those situations, those financial statements must be prepared using the same accounting principles as a public business entity. However, an entity that does not otherwise meet any of the criteria of a public business entity generally would be permitted to apply accounting and reporting alternatives within U.S. GAAP in its standalone financial statements.

BC13. Each definition of the terms *nonpublic entity* and *public entity* in the Accounting Standards Codification includes a criterion that in order to be defined as a nonpublic entity, an entity must not have securities that trade in a public market either on a stock exchange or in an over-the-counter market. Of all the conditions referenced in the definitions of a nonpublic entity over time, the notion of "publicly traded" has been a main factor for making the distinction.

BC14. The Board discussed and considered alternatives that would clarify what is considered to be a public market for securities as it relates to entities that have debt or equity securities. Part of the considerations included (a) whether the

public availability of U.S. GAAP financial statements should be used as a criterion to determine which business entities should be considered public and (b) what is a public market as it relates to business entities that have securities that are able to be resold in a secondary market.

BC15. The Board decided that, consistent with the existing definitions of a nonpublic entity and public entity in the Accounting Standards Codification, entities that have unrestricted securities that are or can be traded on an exchange or an over-the-counter market should be considered public. The Board also added an additional criterion to the definition of a public business entity and decided that if a business entity's securities are unrestricted, and that by law or regulation must provide U.S. GAAP financial statements to be made publicly available on a periodic basis, that entity should be considered public. The Board added this criterion because of the evolution of the markets, which have changed considerably since the existing definitions of a nonpublic entity and public entity were first established. The existing definitions of a nonpublic entity and public entity in U.S. GAAP focus only on securities that trade on a stock exchange or an over-the-counter market.

BC16. Some Board members expressed concern that if the public availability of U.S. GAAP financial statements was used in the definition, entities could be required to reassess their status on an interim or annual basis to determine whether they meet the criteria to be defined as a public business entity. Some Board members who support defining an entity as public on the basis of whether it has U.S. GAAP financial statements that are made publicly available noted that including reference to a legal or regulatory requirement to make financial statements publicly available on a periodic basis would result in entities not needing to reassess whether they meet the definition of a public business entity on a regular basis.

BC17. Another Board member was concerned that limiting the definition of a public business entity to entities that had securities that trade in a public market and make their U.S. GAAP financial statements publicly available would be too restrictive, because entities that have access to the public markets have similar transactions in securities and should not be treated differently on the basis of whether or not their U.S. GAAP financial statements are made publicly available. Many entities provide U.S. GAAP-like information to investors rather than a complete set of U.S. GAAP financial statements. Investors are made aware of the risks in the stocks on the basis of corporate and financial disclosure that is made available. These entities have users that have similar information needs as investors and analysts of public company debt and equity investors. These entities have availed themselves of the benefits provided by issuing securities in the public market and, therefore, should be required to apply the same requirements as public companies.

BC18. The Board decided that the definition of a public business entity should include only unrestricted securities because many private companies place restrictions on the sale of their securities in a secondary market and can control

to whom they sell their securities. Unrestricted securities can be resold to the public without the company's control and generally have an active market, while restricted securities are generally sold to a limited number and type of investors who often will have a greater ability to access management.

Conduit Bond Obligors

BC19. Most definitions of nonpublic entity in the Accounting Standards Codification exclude an entity that is a conduit bond obligor for conduit debt securities that are traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local or regional markets). When considering whether a business entity that is a conduit bond obligor should be considered a public business entity for financial reporting purposes, the Board assessed the six significant differential factors between public companies and private companies including the number and types of users and typical users' access to management. The Board observed that conduit bond obligors are indirectly accessing the public debt markets. Accordingly, the Board concluded that the users of financial statements of a privately held conduit bond obligor often have similar information needs as investors in public company corporate debt securities and, therefore, financial statements should not reflect differences in accounting and reporting guidance. In addition, conduit bond obligors typically have more financial statement users that have less ability to directly obtain additional material financial information than most other private companies.

BC20. The Board considered an alternative that would include in the definition of a public business entity only those conduit bond obligors that are required to indirectly comply with SEC Rule 15c2-12, *Municipal Securities Disclosure*. Some Board members expressed support for this alternative because entities that are indirectly subject to Rule 15c2-12 typically have conduit bonds that are more widely traded and typically have more financial statement users that have less access to management than conduit bond obligors that are not indirectly subject to Rule 15c2-12. Other Board members rejected this alternative because, in their view, the size of a bond offering should not be a determining factor when considering accounting and reporting differences for private companies but, rather, the fact that those entities are accessing the public capital markets should be a determining factor. Board members acknowledge that some entities that are conduit bond obligors face similar resource constraints as many other private companies and indicated that they would be willing to consider potential deferred effective dates for privately held companies that are conduit bond obligors.

Financial Institutions

BC21. The Board discussed whether a financial institution that does not otherwise meet any of the criteria of a public business entity as defined in this proposed Update should be included in the definition of a public business entity

for financial reporting purposes and, therefore, would not be within the scope of the guide. A financial institution referred to in this proposed Update would be subject to the description in paragraph 942-320-50-1 of the Accounting Standards Codification, which includes banks, savings and loan associations, savings banks, credit unions, finance companies, and insurance entities.

BC22. The Board discussed whether to include all financial institutions in the definition of a public business entity on the basis of public accountability because financial institutions hold and manage financial resources for a broad group of individuals for investment purposes and act in a fiduciary capacity. That notion of public accountability is consistent with the decision reached by the IASB when it finalized its IFRS for SMEs. The Board rejected that alternative because of its view that public accountability applies to many regulated industries and should not be a factor in determining whether an entity is considered public for financial reporting purposes.

BC23. Some Board members expressed concern that if financial institutions were not considered public business entities and, therefore, would be within the scope of the guide, it may not always be appropriate for those companies to apply accounting and reporting alternatives within U.S. GAAP because of the unique needs of some financial statement users of financial institutions. The Board determined that a financial institution would not be included in the definition of a public business entity but could be excluded from the scope for specific accounting and reporting alternatives provided within U.S. GAAP if it is determined that those differences would adversely affect the provision of relevant information to financial statement users. The Board decided that a financial institution could be considered for accounting and reporting alternatives in areas of accounting and reporting that are not specific to financial institutions or that are not particularly relevant to financial statement users of financial institutions.

BC24. Some Board members expressed support for including financial institutions in the definition of a public business entity because of their unique nature but also continuing to evaluate whether financial institutions should be permitted to apply accounting and reporting differences when deliberating individual topics. Those Board members stated that the needs and investment strategies of financial statement users of financial institutions, including depositors and regulators, may differ from the needs of most other users of private company financial statements and, therefore, may require separate consideration depending on the accounting or reporting difference under consideration.

BC25. One Board member expressed concern about additional costs that could be incurred by financial institutions if regulators do not accept accounting and reporting alternatives within U.S. GAAP for private companies. As a result, financial institutions may maintain two sets of accounting records, which may not be cost beneficial.

BC26. The Board considered an alternative that would differentiate financial institutions on the basis of asset size. The Board rejected that alternative because it would be difficult to determine a bright line on the basis of the size of a financial institution when assessing user needs and preparer considerations. In addition, if the Board were to establish a size threshold to correspond with current thresholds created by regulators, those thresholds would be subject to change by the regulators during future periods, which would require the FASB to consider whether to make a corresponding change.

Private Companies That Are Consolidated Subsidiaries of Public Companies

BC27. Some of the definitions of nonpublic entity in the Accounting Standards Codification exclude an entity that is controlled by a public entity. The Board considered whether a U.S. private subsidiary that is controlled and consolidated by a U.S. public company should be permitted to apply accounting and reporting alternatives for private companies when preparing standalone U.S. GAAP financial statements.

BC28. For purposes of consolidation, many private subsidiaries already prepare and provide financial information following U.S. GAAP guidance for public companies to their controlling public company. The Board considered that permitting a private subsidiary to apply accounting and reporting alternatives in recognition and measurement guidance, effective dates, and transition methods may not result in significant benefits to a private subsidiary when preparing standalone financial statements. However, the Board noted that permitting a private subsidiary to apply accounting and reporting alternatives relating to disclosures in its standalone financial statements may provide relevant information to its users of standalone financial statements (often times, a lender to the private subsidiary) while reducing costs. In addition, some Board members concluded that a private company should not be precluded from applying differences in its standalone U.S. GAAP financial statements on the basis of its internal reporting requirements to a parent that is a public company. Some Board members indicated that there could be different materiality considerations when preparing the subsidiary's standalone financial statements compared with the materiality considerations used in preparing consolidated financial statements of the public company parent. Therefore, permitting a private subsidiary to apply accounting and reporting alternatives that are not material to its public parent could be cost beneficial for a private subsidiary and users of its standalone financial statements.

BC29. Some Board members expressed concern about the potential for having conflicting accounting information available in the marketplace because financial statements of a private subsidiary would not reconcile to information about the subsidiary that may be included in consolidated financial statements of the public company parent. However, the Board considered that standalone financial

statements would not be made publicly available to all financial statement users of the public company parent and that, under the draft guide, a privately held subsidiary would be required to disclose that it applied alternatives within U.S. GAAP. Specifically, some Board members expressed concerns about considering a wholly owned subsidiary of a public company as a private company because, in some cases, the private subsidiary's operations may be a substantial portion of the public company's financial results. Concerns were raised about structuring, including reverse merger situations, when a private subsidiary purchases control of a public company shell and then merges it with the private company. Those Board members indicated that if disclosure is the primary area in which a private subsidiary would achieve cost savings, future disclosure relief may be provided by the disclosure framework project.

A Private Company That Controls a Public Subsidiary

BC30. The Board considered whether a U.S. private company that controls and consolidates a U.S. public company in its financial statements should be permitted to apply accounting and reporting alternatives within U.S. GAAP for private companies. The Board considered if the consolidated entity as a whole has some public equity holders, whether the consolidated entity should be considered a public entity and whether financial reporting would be simplified if an entity is considered public any time there is a public entity in the consolidated group.

BC31. The Board ultimately decided that a private company that controls and consolidates a U.S. public company in its financial statements should not be considered a public business entity and should be within the scope of the guide because the financial reporting requirements of a public subsidiary should not preclude a privately held entity from applying differences in its own financial statements. When evaluating the six significant differential factors, the Board considered that (a) a private company that controls and consolidates a public company and (b) the characteristics of its financial statement users typically are similar to most other private companies. The Board recognized that permitting a controlling private company to apply accounting and reporting alternatives for private companies may not be cost beneficial in all circumstances, specifically when that controlling private company has a significant number of public subsidiaries or when its primary operations consist of holding an investment in one or more public subsidiaries. However, some private companies have a number of private subsidiaries and if a controlling private company is not permitted to apply accounting and reporting alternatives for private companies in its consolidated financial statements, its private subsidiaries would be required to provide the parent with financial information prepared in accordance with public company U.S. GAAP that may be costly to prepare and irrelevant to financial statement users.

Not-for-Profit Entities

BC32. Many of the definitions of a nonpublic entity and public entity in the Accounting Standards Codification include all types of entities, including NFPs. The Board discussed whether a distinction or distinctions between NFPs are necessary and, if so, how that distinction or distinctions between particular types of NFPs might best be made. Given the unique nature of NFPs and many of their users, the Board decided that a public or nonpublic distinction would not be made between NFPs for financial reporting purposes. Instead, the Board would consider whether all, none, or only some NFPs should be permitted to apply accounting and reporting alternatives within U.S. GAAP. The Board would consider factors such as user needs and NFP resources, on a standard-by-standard basis, when determining whether all, none, or only some NFPs will be eligible to apply accounting and reporting alternatives with U.S. GAAP.

BC33. The Board decided that NFPs have many unique characteristics that differ from most other types of public and private companies. The ownership structures of NFPs differ from most private and public companies in that NFPs do not have shareholders. The primary users of an NFP's financial statements include donors and regulators, in addition to creditors. The needs of many of the primary users of NFP financial statements are specific and unique in comparison with the needs of the primary users of both public and private company financial statements. That is why NFPs have specific reporting guidance that is tailored to the unique nature of the entities.

BC34. The Board considered whether to distinguish between NFPs based on (a) whether the NFP issues or is an obligor for conduit debt securities that are traded in a public market consistent with existing U.S. GAAP, (b) whether it receives public donations, or (c) a size threshold. The Board concluded that these alternatives may not be appropriate in all circumstances and may create an ineffective bright-line among NFPs.

Employee Benefit Plans

BC35. Employee benefit plans have unique characteristics that differ from both private companies and public companies. The needs of users of employee benefit plan financial statements are specific and more focused when compared with the needs of financial statement users of both public companies and private companies. Employee benefit plans follow accounting guidance that often is tailored to the unique nature of the plans. After considering those factors, the Board decided that employee benefit plans should not be included in the definition of a public business entity for financial reporting purposes and should not be included in the scope of the guide. Instead, the Board would consider whether all, none, or some employee benefit plans should be permitted to apply accounting and reporting alternatives under U.S. GAAP. The Board would

consider factors such as user needs and resources, on a standard-by-standard basis, when determining whether all or only some employee benefit plans will be eligible to apply accounting and reporting alternatives within U.S. GAAP.

BC36. The Board considered an alternative that would differentiate an employee benefit plan that is sponsored by a private company from an employee benefit plan that is sponsored by a public company. The Board rejected that alternative because it concluded that the factors that differentiate a private company from a public company, particularly related to the types of users and their financial reporting needs, are not applicable to an employee benefit plan regardless of whether the plan is sponsored by a private company or a public company. Also, most users of employee benefit plan financial statements do not have different financial reporting needs based on the ownership structure of the plan sponsor.

Consequential Amendments

BC37. The Board discussed whether to amend the existing definitions of a nonpublic entity and public entity in the Accounting Standards Codification by replacing them with a new definition of a public business entity. The Board acknowledged that eliminating the multiple definitions of a nonpublic entity and public entity in the Accounting Standards Codification could reduce confusion among stakeholders and simplify the definition, which could help reduce complexity in financial reporting. However, the Board decided that the existing definitions of a nonpublic entity and public entity in the Accounting Standards Codification should not be amended at this time. A new definition of a public business entity would be added to the Master Glossary for use in new accounting and reporting guidance. The Board discussed that one of the primary objectives of the project is to identify the types of entities that would be included within the scope of the guide and would be used on a consistent basis in future deliberations about potential accounting and reporting alternatives within U.S. GAAP. To date, most U.S. GAAP differences between public entities and nonpublic entities have been limited primarily to deferred effective dates and exemptions for some disclosure requirements. Effective date differences are only applicable in the period of adoption and would not remain in the Accounting Standards Codification for future periods. Therefore, if the existing definitions of a nonpublic entity are not amended, this would result in a limited amount of disclosure differences that may potentially be amended over time.

BC38. The Board concluded that amending the existing definitions of a nonpublic entity and public entity would require significant analysis and discussion, regardless of whether the objective is (a) to ensure that the original scope of guidance in the Accounting Standards Codification is preserved or (b) to change the scope of such guidance to align with the new definition. The Board discussed whether to undertake a second phase of the project at a later stage to examine whether to amend current U.S. GAAP with a new definition resulting from this proposed Update. Potential amendments to the definition of a nonpublic

entity and public entity used in ongoing projects (for example, leases or PCC projects) could be evaluated at a later stage once feedback has been received on this proposed Update.

Benefits and Costs

BC39. The objective of financial reporting is to provide information that is useful to present and potential investors, creditors, donors, and other capital market participants in making rational investment, credit, and similar resource allocation decisions. However, the benefits of providing information for that purpose should justify the related costs. Present and potential investors, creditors, donors, and other users of financial information benefit from improvements in financial reporting, while the costs to implement new guidance are borne primarily by present investors. The Board's assessment of the costs and benefits of issuing new guidance is unavoidably more qualitative than quantitative because there is no method to objectively measure the costs to implement new guidance or to quantify the value of improved information in financial statements.

BC40. The Board considered the feedback received from stakeholders, in addition to research performed, to assess how the six significant differential factors that form the basis for the guide should be used for different types of entities. The six differential factors include (1) types and number of financial statement users, (2) access to management, (3) investment strategies of equity investors, (4) ownership and capital structures, (5) accounting resources, and (6) learning about new financial reporting guidance.

BC41. The Board does not anticipate that entities will incur significant costs as a result of the amendments in this proposed Update. The proposed amendments would provide the benefit of improving consistent application of U.S. GAAP by the addition of the term public business entity to the Master Glossary of the Accounting Standards Codification for use in new accounting and reporting guidance. The proposed amendments would not affect existing accounting requirements and would eliminate the use of multiple definitions of nonpublic entity and public entity in new accounting and reporting guidance.

Amendments to the XBRL Taxonomy

The provisions of this Exposure Draft, if finalized as proposed, would not require changes to the U.S. GAAP Financial Reporting Taxonomy (UGT). Any stakeholders who believe that changes to the UGT are required should provide their comments and suggested changes at www.fasb.org.