

# FASB In Focus

## Private Company Decision-Making Framework and Definition of a Public Business Entity

### Background

In May of 2012, the Financial Accounting Foundation (FAF) formed the Private Company Council (PCC), a new body created to improve the process of setting accounting standards for private companies. One of the responsibilities given to the PCC was to work with the FASB, within a mutually agreed upon framework, to determine whether alternatives to existing nongovernmental U.S. generally accepted accounting principles (U.S. GAAP) are necessary to address the needs of users of private company financial statements.

The “mutually agreed-upon framework”—known as the Private Company Decision-Making Framework, or Guide—was first released as a FASB staff paper in 2012 to obtain feedback from various stakeholders. When the PCC was seated, PCC members and the FASB deliberated the feedback received on the staff paper.

One of the critical components to developing the Guide was determining what organizations would be within its scope. The FASB project on defining

a public business entity distinguishes a public company from a private company and addresses some of the organizations that would not be within the scope of the Guide; other organizations not in the scope of the Guide are not-for-profits and employee benefit plans.

As a result of those efforts, on December 23, 2013, the FASB and the PCC issued the final *Private Company Decision-Making Framework: A Guide for Evaluating Financial Accounting and Reporting for Private Companies*. The FASB also issued FASB Accounting Standards Update No. 2013-12, *Definition of a Public Business Entity: An Addition to the Master Glossary*.

The Guide is intended to assist the FASB and the PCC in determining whether and when to provide alternative recognition, measurement, disclosure, display, effective date, or transition guidance for organizations that are within the scope of the Guide, for reporting under U.S. GAAP.

The Definition of a Public Business Entity will be used by the FASB, the PCC, and the Emerging Issues Task Force (EITF) to determine the scope of new financial

accounting and reporting guidance and to identify the types of organizations that are excluded from the scope of the Guide.

### Why Are the FASB and the PCC Issuing the Guide?

The Guide is intended to be a tool to help the FASB and the PCC identify differential informational needs of users of public company financial statements and users of private company financial statements, and to identify opportunities to reduce the complexity and costs of preparing financial statements in accordance with U.S. GAAP.

**The Guide and the Definition of a Public Business Entity are integral parts of the FASB and the PCC's ongoing commitment to better serve the needs of both users and preparers of private company financial statements.**

Additionally, the development of a decision-making framework was one of the most important recommendations included in the *Blue-Ribbon Panel on Standard Setting for Private Companies: Report to the Board of Trustees of the Financial Accounting Foundation*, which was issued in January 2011.

## Why Is the FASB Issuing the Definition of a Public Business Entity?

Defining a public business entity addresses stakeholder concerns about the inconsistency and complexity of having multiple definitions of “nonpublic entity” and “public entity” within U.S. GAAP. The definition will improve U.S. GAAP by providing a single definition of a public business entity for use in future financial accounting and reporting guidance, and will also help clarify the Guide’s scope by defining the types of organizations that are excluded from the Guide’s scope.

## What Are the Guide’s Main Provisions?

The Guide will be used by the Board and the PCC, along with the existing FASB conceptual framework for financial reporting, in making user-relevance and cost-benefit evaluations for private companies.

The Guide describes five significant factors that differentiate the financial reporting considerations of private companies from public companies.

**T**he Guide is intended to be a tool to help the FASB and the PCC identify differential information needs between users of public company financial statements and users of private company financial statements.

Those factors were identified on the basis of an assessment about how and why the needs of users of private company financial statements may differ from users

of public company financial statements. It also summarizes how the cost-benefit considerations of financial reporting may vary between private companies and public companies.

The factors capture the most common characteristics that differentiate financial statement user needs and preparer considerations for private companies from those of public companies:

- The number of primary financial statement users and their access to management
- The investment strategies of primary users
- The ownership and capital structures
- Accounting resources, and
- The manner in which preparers learn about new financial reporting guidance.

The Guide also sets forth five areas (known as modules) where financial accounting and reporting guidance might differ for private and public companies:

- Recognition and measurement
- Disclosures
- Display (presentation)
- Effective dates, and
- Transition method.

## How Does the Guide Differ from the AICPA’s Proposed Financial Reporting Framework for Small- and Medium-Sized Entities?

The AICPA developed a special-purpose framework intended for use by the very smallest, owner-managed private companies that currently do not issue U.S. GAAP

financial statements and would not have any need in the future to prepare U.S. GAAP financial statements—even considering any modifications proposed by the PCC and endorsed by the FASB.

The AICPA’s non-U.S. GAAP approach draws upon a blend of accrual income tax methods and other methods of accounting.

In contrast, the FASB and the PCC will use the Guide to identify alternatives for private companies within U.S. GAAP, based on an evaluation of the needs and characteristics of private company stakeholders.

## What Does the FASB’s Definition of a Public Business Entity Accomplish?

The FASB established which types of organizations would be considered “public business entities” to better distinguish between different types of organizations for standard-setting purposes and to determine which organizations should be included in the scope of the Guide.

**T**he Accounting Standards Codification currently includes multiple definitions of the terms *nonpublic entity* and *public entity*.

The Definition of a Public Business Entity improves U.S. GAAP by providing a single definition of a “public business entity” for use in future financial accounting and reporting guidance.

The Definition of a Public Business Entity amends the Master Glossary of the FASB Codification to include one definition of

public business entity for future use in U.S. GAAP.

A business entity (which excludes a not-for-profit organization or an employee benefit plan) 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 (including voluntary filers) 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, other than the SEC.

- c. It is required to file or furnish financial statements with a regulatory agency (foreign or domestic) in preparation for the sale of or for purposes of issuing securities that are not subject to contractual restrictions on transfer.
- d. It has (or is a conduit bond obligor for) securities that are traded, listed, or quoted on an exchange or an over-the-counter market.
- e. Its securities are not subject to contractual restrictions on transfer, and it is required to prepare U.S. GAAP financial statements (including footnotes) and make them publicly available on a periodic basis (for example, interim or annual periods), pursuant to a legal, contractual, or regulatory requirement. An entity must meet all those conditions to meet criterion (e).

An entity may meet the definition of public business entity solely

because its financial statements or financial information is included in another entity's filing with the SEC. In that case, the entity is only a public business entity for purposes of financial statements filed or furnished with the SEC.

The definition does not affect existing requirements but will apply to new guidance. There is no actual effective date for the term public business entity. However, the term will be effective with the first Updates that use the definition of a public business entity. These are expected to be the final Accounting Standards Updates on the first two PCC consensuses—on accounting for goodwill and on the simplified hedge accounting approach for certain interest rate swaps—in January 2014.

Additionally, the definition is not expected to create any new differences between U.S. GAAP and International Financial Reporting Standards. ■

**For more information about the project, please visit the  
FASB's website at [www.fasb.org](http://www.fasb.org).**