

MINUTES OF THE APRIL 17, 2020 PRIVATE COMPANY COUNCIL MEETING

Location: Remote meeting; broadcast live on the FASB website

Meeting Date: Friday, April 17, 2020

Starting Time: April 17, 2020, 10:00 a.m. EDT

Concluding Time: April 17, 2020, 1:00 p.m. EDT

PCC Members Present:

Candace Wright (Chair)

Zubin Avari

Timothy Curt

Jeremy Dillard

David Lomax

Michael Minnis

Holly Nelson

Richard Reisig

Dev Strischek

Yan Zhang

PCC Members Absent:

Frank Tarallo

FASB Board Members Present:

Russell Golden (Chairman)

James Kroeker (Vice-Chairman)

Christine Botosan

Gary Buesser

Susan Cospers (FASB – PCC Liaison)

Marsha Hunt

Hal Schroeder

Rich Jones (Incoming FASB Chairman)

FASB Staff Present:

Shayne Kuhaneck

Jeffrey Mechanick

Jenifer Wyss

Demi Fritz

Autumn Zobrist

*James Starkey

*Mary Mazzella

*Jill Switter

*Chris Roberge

FAF Representatives Present:

Diane Rubin, FAF Trustee

*For certain issues only.

Introductory Remarks

1. The PCC chair welcomed PCC members, FASB members, and FASB staff to the Council's April meeting, which was held remotely because of the COVID-19 pandemic.

Town Hall Update

2. The FASB staff provided a summary of upcoming Town Hall and Outreach Meetings:
 - The PCC Town Hall Meeting to be held during the AICPA G400 Community Meeting in May has been cancelled as a result of the conference, in its entirety, being cancelled.
 - The June AICPA Engage Conference has been adjusted to an online-only event. In connection with the National Advanced Accounting and Auditing Technical Symposium (NAAATS) program, a PCC Town Hall Meeting will be held during the week of July 20. More details will be forthcoming.
 - The FASB staff and the Risk Management Association (RMA) Accounting and Tax Committee are working to identify a date for a PCC outreach meeting. If an in-person meeting cannot be arranged, a virtual meeting will be considered.

PCC Issue No. 2018-01, "Practical Expedient to Measure Grant-Date Fair Value of Equity-Classified Share-Based Awards"

3. PCC and Board members discussed the progress of a potential practical expedient that would allow a nonpublic entity to determine the current price input of equity-classified share-option awards using a valuation method performed in accordance with the presumption of reasonableness requirements of Section 409A of the U.S. Internal Revenue Code. In February 2020, the Board endorsed the PCC's decision to issue a proposed Accounting Standards Update on that practical expedient. Because many private company stakeholders currently are experiencing resource constraints and may be unable to provide feedback at this time, the PCC unanimously agreed to delay the issuance of the proposed Update until later in the second quarter of 2020.

Revenue Recognition

4. The FASB staff provided an update on the implementation progress of Topic 606, Revenue from Contracts with Customers. The FASB staff highlighted several available resources on the FASB website for entities implementing Topic 606, including the Revenue Recognition Implementation Q&As document issued in January 2020. The FASB staff also updated the PCC on the recent trends of technical inquiries on implementing the revenue recognition standard.
5. The FASB staff updated PCC members on the recent Board decision to add a project to its technical agenda to defer the effective date of Topic 606 for franchisors that are not public business entities, to annual reporting periods beginning after December 15, 2019, and interim reporting periods within annual reporting periods beginning after December 15, 2020. An exposure draft will be issued soon for public comment.

6. Additionally, the FASB staff provided background on the new research project to evaluate how to reduce implementation costs related to applying Topic 606 to initial franchise fees received by franchisors, and PCC members discussed their experience with franchise arrangements.
7. The PCC chair asked whether a practical expedient to reduce implementation costs for franchisors had been developed and whether that practical expedient would be available to private company franchisors that elect to defer the application of Topic 606. FASB staff explained that the potential practical expedient would be expected to apply not only to private company franchisors but would provide relief to the entire industry. Furthermore, the potential practical expedient would be expected to apply to all franchisors regardless of whether they elect to delay their Topic 606 adoption.
8. A PCC member asked whether there were any specific industries affected. FASB staff noted that franchise arrangements can occur in any industry. FASB staff emphasized the importance of determining whether the value of the services provided are directly attributable to the brand.
9. A PCC member noted that his clients struggle with determining the standalone selling price related to initial franchise fees (for example, the standalone selling price of training) and encouraged the FASB to provide help on how to establish that standalone selling price. That PCC member also suggested simplifying the accounting for the transition adjustment related to long term franchise agreements. The accounting for long term agreements can be complicated and result in looking back over many years to the origin of the agreement to calculate the transition adjustment.

Conceptual Framework – Elements, Measurement, and Presentation

10. The FASB staff provided an overview of the three conceptual framework projects: Elements, Measurement, and Presentation. The FASB staff described the history of the conceptual framework projects and ways in which the three projects are interrelated. An exposure draft was issued in 2016 on the Presentation project. That project has been put on hold while issues relating to the Elements project are being resolved.
11. The Measurement project has been discussed extensively by the Board, but no significant decisions have been made. An Invitation to Comment for the Measurement project is planned for late 2020, and FASB staff encouraged the PCC to provide feedback.
12. The FASB staff then discussed the Elements project and the proposed revisions to the definitions of *assets*, *liabilities*, *revenues*, *expenses*, *gains*, and *losses*. An exposure draft on the Elements project is planned for late 2020 and FASB staff encouraged PCC members to provide feedback.
13. The PCC chair asked whether the Board expected the population of items that currently meet the definitions of *assets* and *liabilities* to change. The FASB staff noted that such a

question would be included in the exposure draft and that the Board would expect changes with respect to internally generated intangible assets and to some share-settled debt. PCC members asked questions about the classification of certain arrangements in which debt is settled in shares. A Board member clarified that the conceptual framework is a tool used by the Board to contemplate standard setting. Therefore, any changes to practice would be as a result of standard setting projects.

14. Some PCC members disagreed with the FASB staff's statement that a cost basis of measurement was less clearly defined than fair value. FASB staff noted that there are differing views about which amounts should be included when using a cost basis of measurement. In contrast, the amounts included in a fair value analysis may be more consistently understood. A Board member suggested that in some situations fair value may be easier to apply than cost.

Current Issues in Financial Reporting

15. PCC members discussed issues arising as a result of current business conditions under the COVID-19 pandemic. Additionally, the FASB staff provided an update on several emerging issues affecting private companies, including:
 - a. **Leases:** The Board decided to amend the effective date of Topic 842, Leases, for private companies and private not-for-profit entities to annual reporting periods beginning after December 15, 2021, and to interim periods within the fiscal years beginning after December 15, 2022. An exposure draft will be issued soon for public comment.
 - b. **Fair Value Measurement:** An agenda request was received to suspend mark-to-market accounting. FASB staff provided a reminder of the orderly transaction guidance in Topic 820, Fair Value Measurement, specifically paragraphs 820-10-35-54C through 35-54J. FASB staff encouraged PCC members to reach out if they have questions or encounter interpretation issues with the existing guidance.
 - c. **Interest Income Recognition:** The Board recently discussed a technical inquiry received by the FASB staff regarding the recognition of interest income. For illustrative purposes that inquiry included a fact pattern whereby an institution was providing assistance to borrowers affected by the COVID-19 pandemic. FASB staff acknowledged two appropriate views for accounting for interest income.
 - d. **Small Business Administration Loans:** FASB staff noted that questions are arising related to lender accounting for fees received and borrower accounting for loan forgiveness. FASB staff noted that business entities, which are scoped out of Accounting Standards Update No. 2018-08, *Not-for-Profit Entities (Topic 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*, for transfers of assets from governmental entities, are not precluded from applying the guidance by analogy when appropriate.

Additionally, the FASB staff has had ongoing dialogue with both the AICPA and practitioner groups preparing to publish papers discussing those issues.

16. A PCC member shared feedback from stakeholders requesting the ability to early adopt some (but not all) of the simplification provisions of Accounting Standards Update No. 2019-12, *Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes*. That PCC member also noted that private companies are currently experiencing operational difficulties in computing the tax effect of the changes to deferred taxes, valuation allowances, and effective tax rates resulting from recent changes in tax laws.
17. PCC members reported that preparers are experiencing difficulties under the current circumstances with fair value measurement and expressed their appreciation for the FASB staff drawing attention to the orderly transaction provisions of Topic 820, Fair Value Measurement. FASB staff encouraged stakeholders to contact the FASB for assistance in understanding the guidance applicable to specific fact patterns. If issues are pervasive, the FASB can consider issuing question-and-answer documents.
18. PCC members also reported that preparers are experiencing difficulties under the current circumstances with evaluating whether there is substantial doubt about an entity's ability to continue as a going concern. PCC members encouraged the Board and FASB staff to provide additional guidance on going concern analyses.
19. PCC members noted that private companies are experiencing difficulties under the current circumstances determining what is required to be disclosed and the appropriate level of detail for disclosures. PCC members noted that users want sufficient disclosures to assess the effects of current circumstances on an entity. PCC members suggested that the FASB or AICPA develop additional educational materials related to disclosure requirements.
20. As a means to address some of the educational aspects of the issues arising as a result of the COVID-19 pandemic, the PCC suggested that the FASB provide a webcast for private companies addressing issues related to the current business environment. The Board and FASB staff noted ongoing efforts to monitor the marketplace and coordinate with the profession to ensure there is an appropriate level of guidance and support for private companies.

Private Company Research Findings

21. The PCC member from Academia presented some of his private company research findings. With regard to the correlation between the incidence of audited GAAP financial statements and a number of identifiable factors, the findings reveal that: (a) equity and debt capital and trade credit exhibit significant explanatory power, (b) firm youth, growth, and research and development are positively associated with audited GAAP reporting, and (c) many firms violate standard explanations for financial reporting choices and substantial unexplained heterogeneity in financial reporting remains.

22. PCC and FASB members discussed the trends of audited GAAP-based financial statements for private companies and the rationale for why private companies have their financial statements audited, as well as some benefits they appear to receive from doing so.
23. Two PCC members noted that from their experiences, audited financials were required based on a bank's size and risk exposure. Larger banks more often required audited financial statements from borrowers while smaller banks more often used compiled or reviewed financial statements from borrowers. One PCC member observed that in general, companies that produced audited financials had higher levels of revenue and profitability. That member also noted that credit scores and tax returns sometimes were more relied upon than the financial statements in deciding whether to extend credit.
24. In response to these observations, the PCC Academic noted that there are studies for which the benefits of audited financials are still unknown. He also highlighted that ownership structure is a contributing factor for the occurrence of GAAP reporting. Since private equity has grown since a study was done in 2010, he expects that private equity firms would have a strong positive correlation to investing in firms with audited financials.
25. Another PCC member noted that from a surety perspective, in theory, more credit might be extended to those companies that had an audit performed versus a review. Additionally, that member observed a trend that after the 2008 Financial Crisis and large losses being recognized in income statements in 2012-2013, there was an increase in audit requirements.
26. PCC members noted that the relationship a lender has with its customer could influence whether an audit is required. The size of the bank also could influence whether a company is required to have an audit. Furthermore, the requirement for a company to have an audit might be indicative of the lender's experience and the lender's ability to understand the financial statements.
27. One Board member asked about the relationship between intangible assets and the usefulness of GAAP-based financial statements. From his research, the PCC Academic found that firms in industries with more booked and non-booked intangible assets are more likely to have audited financial statements.