

## MINUTES OF THE DECEMBER 11, 2014 PRIVATE COMPANY COUNCIL MEETING

Location: FASB Offices  
401 Merritt 7  
Norwalk, Connecticut

Thursday, December 11, 2014

Starting Time: 8:30 a.m.

Concluding Time: 2:15 p.m.

### **PCC Members Present:**

Billy Atkinson, Chairman  
George Beckwith  
Steve Brown  
Jeffery Bryan  
Mark Ellis  
Thomas Groskopf  
Neville Grud  
Carleton Olmanson  
Diane Rubin  
Larry Weinstock

### **FASB Board Members Present:**

Russell Golden  
James Kroeker  
Daryl Buck  
Harold Schroeder  
Marc Siegel  
Lawrence Smith  
Thomas Linsmeier

### **FASB Staff Present:**

Michael Cheng  
Susan Cospers  
Kelsey Jensen  
Jeffrey Mechanick

\*Elizabeth Gagnon  
\*Regenia Cafini  
\*Sean May  
\*Victoria McMillen  
\*Cullen Walsh  
\*Matthew Silver  
\*Cullen Walsh  
\*Jennifer Hillenmeyer  
\*Adam Smith  
\*Nick Burgmeier

\*Mary Mazzella  
\*Rosemarie Sangiuolo  
\*Michael Cahill  
\*Nick Malone  
\*Jack Pohlman  
\*Matt Esposito

\* For certain issues only.

## **INTRODUCTORY REMARKS**

The Private Company Council (PCC) discussed its plans for outreach in 2015. The PCC announced that its first town hall for 2015 will be held on April 28, 2015 at Southern Methodist University in Dallas, Texas. The Texas Society of Certified Public Accountants will assist with planning and hosting this town hall.

John Davidson, Vice Chairman of the Financial Accounting Foundation (FAF), made comments thanking the PCC members for their commitment to working with the FASB to improve financial reporting—not only for private companies, but also for the wider financial reporting community. He emphasized the mutual collaboration between the PCC the FASB and the importance the PCC places on seeking stakeholder input. He noted that the PCC has made significant progress addressing issues identified as critical by private companies and that it has continued to provide value-added input on FASB projects. The FAF's assessment of the PCC's operations will occur over the next year.

## **DISCUSSION OF PRIVATE COMPANY COUNCIL PROJECTS**

### *Definition of a Public Business Entity (Phase II)*

The PCC discussed the ramifications of replacing the Codification definitions for Nonpublic Entity/Public Entity and Public Entity (Definitions 4 and 5, respectively, in Appendix A of Memo No. 1 for this Issue) with the new definition of a Public Business Entity (PBE). By replacing the existing definitions, the definition of a PBE could reduce confusion among stakeholders and simplify the Codification, which could help reduce complexity in financial reporting.

Definition 4 affects Topic 740, Income Taxes, while Definition 5 affects Topic 280, Segment Reporting, and Topic 805, Business Combinations. The purpose of the discussion was to inform the PCC about the entities that would likely be affected by this change by becoming either private or public entities, and for the PCC to provide direction on how to proceed with Phase II.

Several PCC members expressed the view that they would like to see a common definition used while still maintaining the original scope within each Topic. Therefore, the PCC asked the FASB staff to analyze the feasibility of using the new definition of a PBE while maintaining the scope of each respective topic for consideration at its next meeting.

### *Partnership Accounting*

The FASB staff provided updates on two issues relating to partnership accounting:

- *Issue 1 - Applying the goodwill method (that is, pushdown accounting) when there is a change in partnership interest. Prior to Accounting Standards Update No. 2014-17, Business Combinations (Topic 805): Pushdown Accounting, there was no guidance in*

GAAP on when to apply pushdown accounting. Outreach with private company constituents indicated that many private companies followed SEC guidance (SAB Topic 5.J) in determining when pushdown accounting was appropriate. Some preparers and practitioners indicated that pushdown accounting for a partnership was applied when a change in control occurred. While rare, some preparers and practitioners also stated that pushdown accounting is applied in instances in which there is just a change in partnership interest without a change in control. With the issuance of Update 2014-17, the PCC concluded that there should no longer be a practice issue in determining when the goodwill method (pushdown) is permitted for partnerships.

- *Issue 2 - Accounting for payments made to partners who provide significant services to a partnership.* Preliminary outreach indicated that some partnerships account for such payments as compensation while other partnerships account for such payments as equity distributions. Some private company constituents raised concerns that there is no guidance in GAAP to account for such payments and that users of private company financial statements may not be aware of the diversity in practice. The PCC members representing users responded that they are aware of this diversity in practice and believe that the financial statements provide sufficient information for follow-up questions. For example, one PCC member stated that he usually reviews compensation expense and any related-party disclosures. If compensation appears to be significantly above or below market rate he usually performs additional follow up with management. The PCC decided not to pursue this issue any further because PCC members representing users indicated that a change in this area is not warranted.

During the discussion, one PCC member was particularly concerned with the effective date of Update 2014-17, which is immediately upon issuance on November 18, 2014. That PCC member was concerned that private companies that are unaware of the immediate effective date will continue to apply pushdown accounting to partnerships even though a change in control event has not occurred. The PCC asked the FASB staff to utilize its communication channels with the private company community to inform preparers and practitioners of the effective date.

The PCC also asked the FASB staff to continue its research on partner contributions of non-monetary assets for discussion at a future meeting.

### *Share-Based Compensation*

The FASB staff provided an update and asked for feedback from the PCC regarding the practical expedients for private companies that the staff brought to the Board at an earlier non-decision making meeting. The topics brought forth for private companies included:

- Simplifying the Determination of the Expected Term in the Black Scholes model

- Classification of Awards with Repurchase Features
- Additional Opportunity to Elect Intrinsic Value for Existing Liability-Classified Awards
- Entities Permitted to Apply Private Company Practical Expedients.

Several PCC members expressed their concern that the current number shown as compensation expense on the income statement is very difficult to calculate and does not provide relevant information. They suggested that private companies be allowed to classify all awards as liabilities with measurement based on intrinsic value. They also suggested that this alternative should allow private companies to make use of formula value repurchase features when valuing the underlying shares.

Several PCC members indicated that something should be done to reduce the current disclosure requirements for share-based payments. They suggested that decreasing the amount of disclosures could reduce the current cost of complying with the share-based payment accounting requirements. The Board directed the staff to conduct additional research regarding share-based payment disclosures as part of the Disclosure Framework project.

## **DISCUSSION OF PCC AGENDA TOPICS**

The topics discussed by the PCC with input from the FASB staff included:

- Current and Potential FASB Topics
  - Simplifying Accounting for Asset Retirement Obligations
  - Employee Benefit Plans
  - Deferred Taxes: A FASB Board member stated that the Post-Implementation Review of deferred taxes concluded that the standard is, overall, effective and that the current project is focused on simplifications to accounting for income taxes.
  - Financial Performance Reporting: One PCC member noted the growing use of non-GAAP measures, such as EBITDA, and believes that the presentation and display of financial information is being underutilized as a result. That PCC member proposed a project that would improve relevance but would not change any recognition or measurement criteria.
- Potential PCC Topics

- Variable Interest Entities—Brother-Sister Operating Entities: One PCC member noted that there is diversity in practice in identifying the primary beneficiary for brother-sister entities operating under common control.

## **ADVISORY DISCUSSION OF FASB PROJECTS**

### *Simplifying Inventory*

The FASB staff provided an update and asked for feedback from the PCC on the recent decision to measure inventory at the lower of cost and net realizable value.

One PCC member asked whether, as part of its simplification discussions, the Board considered no longer allowing inventory to be measured on a last-in-first-out (LIFO) basis. The staff explained that the project is intended to be narrow and that eliminating a currently acceptable method of inventory accounting is beyond the scope of this project. One Board member stated that if the Board were to no longer allow inventory to be measured on a LIFO basis, such action would have a tremendous economic impact because of the tax consequences.

### *Business Combinations and Related Issues*

The FASB staff provided an update on accounting for goodwill for public business entities and not-for-profit entities. The Board recently decided to add a project to its agenda for public business entities and not-for-profits as a result of PCC Issue No. 13-01A, "Accounting for Identifiable Intangible Assets in a Business Combination," which resulted in private companies no longer recognizing customer-related intangible assets that are not capable of being sold or licensed independently from the other assets of the business and all non-competition agreements entered into in connection with a business combination.

The Board has instructed the staff to perform additional research on the amortization of goodwill, including identifying the most appropriate useful life, as well as research on simplifying the impairment test of goodwill.

One PCC member asked whether U.S. GAAP was converged with IFRS regarding the recognition and subsequent impairment of goodwill. The staff explained that the current overall model was consistent with IFRS but there are some inconsistencies with application (for example, a two-step impairment test [GAAP] versus a one-step impairment test [IFRS], impairment assessment at reporting unit level [GAAP] versus cash generating unit level [IFRS]).

### *Definition of a Business*

The FASB staff provided an update and asked for feedback from the PCC regarding various aspects of the project including clarifying the definition of a business, clarifying accounting for

partial sales and retained interests, and considering whether other asset-versus-entity differences can be eliminated.

One PCC member asked the staff to comment on any decisions made regarding in-substance nonfinancial assets. The staff explained that those assets have been scoped into the project and will be addressed in the second phase of the project.

#### *Liabilities and Equity—Short-term Improvements*

The FASB staff provided an update and asked for feedback from the PCC regarding the scope of the project. The scope includes: determining whether an instrument is indexed to an entity's own stock (down-rounds); the indefinite deferral in Topic 480 related to certain mandatorily redeemable financial instruments; freestanding contracts indexed to, and potentially settled in, an entity's own stock; and improving the navigation of the Codification.

One PCC member questioned whether down-rounds are fairly prevalent transactions. Another PCC member stated that they have seen many down-round transactions and that the current accounting is counter-intuitive. That PCC member is supportive of Codification navigation improvements and, as part of that effort, explaining the application of the indefinite deferral in Topic 480.

#### *Accounting for Financial Instruments—Impairment*

The FASB staff provided background on the project and discussed how the current expected credit loss model would be applied. The FASB staff discussed feedback received, tentative Board decisions reached through redeliberations, and the project timeline. The FASB staff asked for the PCC's feedback regarding the recognition of day one expected losses.

#### *Accounting for Financial Instruments—Classification and Measurement*

The FASB staff provided an update and asked for PCC feedback regarding the redeliberated model for classifying and measuring financial assets and liabilities.