

Private Company Financial Reporting Committee

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JUDITH H. O'DELL
Chair

Meeting Highlights April 29-30, 2010

Norwalk, Connecticut

All Private Company Financial Reporting Committee (“PCFRC” or “Committee”) members were in attendance.

Financial Accounting Standards Board (“FASB”) Board Member: Leslie Seidman, Staff: Paul Glotzer

American Institute of Certified Public Accountants (“AICPA”) Staff: Bob Durak

April 29th Meeting with FASB members

On April 29th, the PCFRC met with members of the FASB. Highlights of that discussion follow:

- Introduction of new PCFRC members. The following new members of the PCFRC were introduced:
 - George W. Beckwith, National Gypsum Company (preparer member)
 - Stephen Bodine, LarsonAllen LLP (practitioner member)
 - Steven D. Lords, Martin-Harris Construction Company (preparer member)
- Nonpublic Entity Considerations in the Standard Setting Process. FASB Assistant Director Jeff Mechanick informed the PCFRC about a new formalized policy at the FASB to improve the process for receiving quality input to ensure that the financial reporting needs of nonpublic entities are adequately addressed. Among the steps included in the policy are the following:
 - The FASB staff will seek input specifically from those involved in financial reporting for nonpublic entities, including users, preparers, and CPA practitioners. This will provide a better understanding of the effect of accounting alternatives and the potential effect of standard-setting activities on nonpublic entities.
 - During the standard-setting process, the FASB staff will provide the members of the FASB with alternatives for nonpublic entities. These alternatives will be based on differences in user needs and cost-benefit considerations.
 - The FASB will articulate within the basis for conclusions section of standard setting documents, both Proposed and Final Accounting Standards Updates (ASUs), the basis for its decisions on whether differences should exist for recognition, measurement, disclosure, transition, or effective date for nonpublic entities.

- As part of the FASB's due process for standard-setting activities on Proposed ASUs, the Board will explicitly request information on the standard's impact on nonpublic entities.
- Following the FASB's receipt of comment letters, the FASB will analyze and evaluate whether differences are warranted for nonpublic entities.
- Why FASB members would consider differential accounting for private companies. The PCFRC inquired of FASB members about the circumstances that would need to be present for those Board members to consider differences in accounting for private companies. Responses from FASB members were mixed and included the following:
 - Disclosure differences could be warranted based on the degree to which the required disclosures in a standard were useful to private company financial statement users.
 - Differences in recognition and measurement principles are difficult to justify. One FASB member was willing to consider differences in recognition and measurement principles if private companies had different capital structures.
 - Differences in the effective date of a new standard and transition guidance may be warranted for private companies on a case-by-case basis.
 - Compliance costs and user needs are important considerations when deciding upon differential accounting for private companies.
 - FASB reaches out to private company financial reporting users but broad-based input is not received.
 - Having separate standards for private companies would be costly to financial statement users who are involved with both public and private companies.
- Possible complications arising in convergence projects due to the issuance of International Financial Reporting Standard for Small- and Medium-Sized Entities ("IFRS for SMEs"). Now that the International Accounting Standards Board ("IASB") has separated private company accounting standards from public company standards with the issuance of IFRS for SMEs, the IASB does not need to consider the needs of private company constituents when developing standards related to the convergence projects. The PCFRC asked FASB members if this presented any complications, because the FASB still needs to consider private company constituents in the convergence projects. FASB members suggested that after the IASB and FASB reach joint decisions on the convergence projects, the FASB would separately consider the need for modifications for private companies.
- Public company/regulatory "creep" into private company accounting. PCFRC members expressed concern to FASB members that the issues and regulatory concerns related to the oversight of public companies continues to creep into private company accounting because both public and private companies follow the same set of GAAP. FIN 46R and FIN 48 were cited as examples.
- Prioritizing FASB-IASB convergence projects, consideration of effective dates and due process. PCFRC members offered their advice to the FASB members on some key matters to consider related to the prioritization of convergence projects and their effective dates and related due process. Points made included the following:

- **Financial Statement Presentation Project**
 - The exposure period and outreach effort related to the Financial Statement Presentation project should be greater because of its affect on so many private company constituents. IRS forms, state and local tax forms, and bank covenants will need to be changed to reflect the provisions of the proposed standard.
 - The PCFRC informed the FASB that the Risk Management Association (“RMA”) re-worked financial statements using the guidelines in the Financial Statement Presentation Discussion Paper in an effort to identify the impact of the proposed guidelines on the lending industry. FASB members asked the PCFRC to see if RMA could provide the results of that work to the FASB.
 - The PCFRC expressed concern over the degree of precision that will be needed to comply with the Financial Statement Presentation project’s proposed disaggregation requirements. The more precise, disaggregated financial information proposed in the project may not be auditable in a cost-effective manner. As such, a risk exists that some private companies may not comply with the requirements of the upcoming Financial Statement Presentation standard. FASB should consider making the standard optional for private companies.
 - FASB members suggested that the Board should conduct thorough cost/benefit testing of the proposed Financial Statement Presentation standard during its exposure period to better understand if this proposed standard should apply to the private company sector.
- **Revenue Recognition Project**
 - PCFRC members stressed that the impact of the Revenue Recognition project is critical to the private company sector, especially construction, software, and technology companies.
 - The PCFRC stated that ultimately the project’s merits should be based on whether the proposed standard will increase transparency related to revenue recognition. A FASB member stated that improving transparency is key.
 - PCFRC members stated that certain industry-specific revenue recognition practices should be maintained, especially in the construction industry. FASB members stated that reaching out to different industries and understanding their unique issues is an ongoing challenge. Also challenging is the effort to develop an overriding revenue recognition principle that can be implemented in all those different industries (i.e., one principle with different methodologies).

Comment Letter on Reporting Entity Exposure Draft

On March 11, 2010 the FASB and IASB issued their Exposure Draft, *Conceptual Framework for Financial Reporting: The Reporting Entity*. The PCFRC worked on

developing comment points on the Exposure Draft. The comment letter will be finalized at the June PCFRC meeting. Comment points may focus on the following issues:

- Clarification and guidance is needed about when combining financial statements are appropriate. Often in the private company sector, an individual may own multiple entities. Uncertainty exists about what types of combined financial reporting are acceptable.
- The legal ownership and composition of entities is important to the users of private company financial statements. For example, users may not have access to the cash flows of entities that may be consolidated into a potential group reporting entity but are outside the legal composition of the reporting entity. As such, including the assets, liabilities, operations, and cash flows of such an entity in the financial statements of the reporting entity would not be decision-useful to the user of the reporting entity's financial information.
- The definition of a "reporting entity" in paragraph S1 of the Exposure Draft contains the following words: "A reporting entity is a circumscribed area of economic activities whose financial information has the potential to be useful to existing and potential equity investors, lenders, and other creditors who cannot directly obtain the information they need..." The inclusion of the words "who cannot obtain the information they need..." seems extraneous and would eliminate many private companies from the definition.
- The PCFRC believes that the Reporting Entity portion of the Conceptual Framework should be completed before the FASB and IASB develop their standards on consolidation.
- The PCFRC will consider recommending that parent-only financial statements be allowed for private companies.

Identifying Standards that Add Complexity

Stemming from a discussion held by the Private Company Accounting Blue Ribbon Panel, the PCFRC discussed which existing standards added an inordinate amount of complexity to the preparation of private company financial statements while providing little benefit to the users of those financial statements. Standards and topics identified were:

- FIN 48, Accounting for Uncertainty in Income Taxes (FASB Codification Topic 740)
- FIN 46R, Consolidation of Variable Interest Entities (FASB Codification Topic 810)
- FASB 142, Goodwill and Other Intangible Assets (FASB Codification Topic 350) – specifically the annual testing of goodwill impairment.
- Accounting for financial instruments, derivatives, and hedging
- Fair Value

The PCFRC will continue to develop a list of these standards and topics for future use with the FASB and possibly the Blue Ribbon Panel.

Updates on Key FASB Projects

FASB staff managers provided the PCFRC with updates on key projects, including the following:

- Financial Statement Presentation
- Consolidations
 - The PCFRC will provide FASB staff with common consolidation examples in the private company sector so FASB staff can better understand the kinds of situations that private company constituents may need guidance on.
- Disclosures of Certain Loss Contingencies
- Multi-employer Plans
- Revenue Recognition
- Fair Value
- Financial Instruments
- Leases

Update about Activities of Private Company Accounting Blue Ribbon Panel (“BRP”)

Judy O’Dell (PCFRC Chair), who is a participating observer on the BRP, provided the PCFRC with an overview of the first meeting of the BRP. The Financial Accounting Foundation (“FAF”), the AICPA, and the National Association of State Boards of Accountancy (NASBA) established the BRP to address how U.S. accounting standards can best meet the needs of users of private company financial statements. The BRP will provide recommendations to the FAF on the future of standard setting for private companies, including whether separate, standalone accounting standards for private companies are needed. Information about the BRP meeting can be obtained at <http://www.fasb.org/cs/ContentServer?c=Page&pagename=FASB%2FPage%2FSectionPage&cid=1176156685295>

Update on Activities of the Financial Executives International’s (“FEI”) Private Company Standards Committee

Chris Rogers of the PCFRC talked about the recent activities of FEI’s private company standards committee. FEI’s committee intends to communicate with the PCFRC more frequently in an effort to share information, points of view, and results of its regular surveys of FEI members.

Administrative Matters/Next PCFRC Meetings

The PCFRC spoke with Terri Polley, President of FAF, about the interaction of the PCFRC with the FASB and FASB staff. The PCFRC informed Ms. Polley that interaction with FASB staff has expanded and improved. In addition, the PCFRC expressed pleasure at having a FASB member present throughout the entirety of the PCFRC’s meeting. Having a FASB member add his or her input and knowledge to the discussions taking place engenders a more productive and fruitful meeting.

Tentative PCFRC meeting dates for 2010 are as follows:

- June 24-25, 2010 (Washington, D.C.)
- September 9-10, 2010 (TBD)
- December 2-3, 2010 (Norwalk, Connecticut)