AICPA® PCPS
Private Companies Practice Section

July 2015

Technical Issues Alert

Information on technical issues affecting small businesses and the CPAs who serve them.

TIC Meets with Peer Review Board

The state of practice monitoring was a key topic when TIC held a liaison meeting with the AICPA Peer Review Board. Issues discussed included:

- *Short-term plans for addressing audit quality.* The two groups covered issues in regulatory and nonregulatory audits, the training and availability of qualified peer reviewers and resolving common peer review deficiencies. TIC members offered perspectives based on their own experiences.
- *The future of practice monitoring*. The AICPA has created a concepts paper and other resources addressing this issue. The two groups discussed the logistics of some proposals and how they would work in practice.
- *Recent and planned standard-setting efforts*. The groups discussed peer review issues related to SSARS 21, *Statements on Standards for Accounting and Review Services: Clarification and Recodification*, and the rescission of Technical Practice Aid 5250.15 (see separate story in this issue).

Elsewhere, the Peer Review Board also finalized its November 2014 ED, *Preparation of Financial Statements Performed under SSARS and the Impact on Enrollment in and the Scope of Peer Review*, which TIC generally supported in its comment letter. The board concluded that firms that only perform preparation engagements under AR-C Section 70, *Preparation of Financial Statements*, would not be required to enroll in the AICPA peer review program. However, a firm's preparation engagements would be included in the scope of a peer review when the firm either elects to enroll in the program (e.g., to comply with licensing or other requirements) or is already enrolled due to other engagements it performs. ■

PCAOB Proposal on the Use of Specialists Could be Detrimental to Smaller Firms

The *TIC Alert* does not normally report on proposals issued by the PCAOB. However, we are making an exception for PCAOB Staff Consultation Paper No. 2015-01, *The Auditor's Use of the Work of Specialists*. If your firm performs audits of public companies and uses the work of specialists, we encourage you to read and comment on this consultation paper.

The use of specialists in the audit of public companies is no longer confined to highly technical applications in specialized industries. Experts are also needed to develop accounting estimates, including fair value estimates, for a number of complex transactions for an increasing number of businesses. The PCAOB believes that the current audit standards may not be rigorous enough to address the risks of material misstatement inherent in the audit of accounting estimates and wants to update its standards to ensure that public company auditors are using the work of a specialist appropriately.

continued on page 2

FUTURE MEETINGS

TIC meetings offer local practitioners the chance to provide their unique perspectives in the standard-setting process. All CPAs are invited to attend. Contact Linda Volkert, CPA, TIC Staff Liaison, at the AICPA at (212) 596-6040 to learn about attending or receivig information on upcoming meetings.

The next TIC meetings will be held:

- September 23 and 24, Norwalk, CT. TIC's annual liaison meetings with the FASB, GASB and PCC.
- October 27 and 28, Point Clear, AL. Includes a liaison meeting with the AICPA Accounting and Review Services Committee.

The PCPS Technical Issues Committee (TIC) provides standard setters with the unique perspective of local CPA firms on accounting, auditing and reporting issues. We hope these highlights of issues that affect local firms will help you, your firm or your group to participate in the standard-setting process.

continued from page 1

Certain aspects of the paper affect all firms that use the work of specialists that are engaged by or employed by the public company (a company's specialist). Today, the auditor turns to AU sec. 336, *Using the Work of a Specialist*, for guidance on the procedures to be performed. Under this standard, the auditor obtains an understanding of the assumptions and methods used by the specialist, performs certain tests of the data provided to the specialist and ensures that the financial statement amounts are consistent with the specialist's findings. The PCAOB staff is considering requiring the auditor to evaluate evidence provided by a company's specialist similarly to other evidence provided by the company to the auditor, which would effectively involve reperformance of the specialist's work by the auditor.

Under the theory that the work of a specialist hired or employed by management is equivalent to management information, the PCAOB staff is considering a new requirement for auditors to evaluate the reasonableness of the significant assumptions and the appropriateness of the methods used by the specialist. If an auditor did not have the requisite knowledge or skills to perform these additional procedures or if the specialist refused to provide information on its assumptions and methods to the auditor, the audit firm might need to employ or engage its own specialist. Large firms may be able to look to their internal specialists, but smaller firms that do not have such in-house expertise would have to engage outside specialists, creating a disproportionate cost burden for the smaller firms and their clients.

Furthermore, additional provisions of the paper would be especially detrimental for smaller firms that engage a third-party specialist (the auditor's specialist). The PCAOB staff wants to strengthen current standards by requiring auditors to verify that third-party specialists adhere to the SEC independence rules and by requiring auditors to perform additional procedures to enhance supervision of the specialist's work. If the specialists have to comply with the independence requirements, their ability to provide services to clients, including audit firms, may be reduced, potentially increasing the costs to the firms looking to engage a specialist. The key issue is whether smaller firms would be capable of implementing these proposed requirements and, if not, how their practices would be affected.

The PCAOB staff is seeking as much input as possible on how smaller firms are currently obtaining evidence regarding the use of specialists and how the proposals in the consultation paper could affect them. The PCAOB staff suspects that the proposals could be too onerous for smaller firms, but as of now, it does not have evidence to support this view. If your firm performs public company audits and would be adversely affected by the proposal, please consider sending a comment letter to the PCAOB by the July 31 deadline. ■

TIC Discusses Issues with FASB Staff

TIC conducts regular meetings with FASB staff members to gain insights into FASB projects and offer the practitioner's perspective. During their most recent meeting:

- TIC and FASB staff members reviewed ongoing research on preferability issues related to the first election of a PCC accounting alternative. Some of the guidance discussed included ASUs No. 2014-02, *Intangibles—Goodwill and Other (Topic 350)*; No. 2014-03, *Derivatives and Hedging (Topic 815)*; and No. 2014-07, *Consolidation (Topic 810).* TIC believes the PCC should reexamine the preferability rules for private entities and consider allowing private entities to choose initial election of a PCC alternative at any time after the effective date of a FASB ASU without a requirement to assess preferability.
- In a discussion on the FASB's disclosure review, topics included existing confusion about what materiality is and how to apply it and recent board decisions on fair value disclosures.
- The FASB staff members encouraged TIC and the members' individual firms to comment on the ED, *Presentation of Financial Statements of Not-for-Profit Entities* (see separate article in this issue). To supplement the ED, the FASB has made available a FASB in Focus article, a frequently asked questions document and an educational webinar.
- TIC and FASB staff discussed revenue recognition amendment EDs, including proposed ASU *Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing*, which has been issued; and another expected proposal on narrow scope improvements and practical expedients.
- In addressing the FASB project on simplification of the balance sheet classification of debt, TIC offered to perform a survey of financial statement users that would be similar to one TIC provided to the FASB in 2004 when this topic was on the board's agenda. TIC opposes the current proposal and has encouraged the FASB staff to perform more extensive research involving users of private company financial statements. ■

CPEA Efforts Result in Elimination of Disclosure of Open Tax Years When No Unrecognized Tax Benefits Exist

As a result of investigative work conducted by the PCPS Center for Plain English Accounting (CPEA), Technical Practice Aid (TPA) 5250.15, which required an entity to disclose a description of tax years that remain subject to examination regardless of whether an entity has any uncertain tax positions (i.e., unrecognized tax benefits), has been deleted. TIC serves as the advisory board for the CPEA.

FASB Accounting Standards Update (ASU) 2009-06, *Implementation Guidance on Accounting for Uncertainty in Income Taxes and Disclosure Amendments for Nonpublic Entities*, was released in 2009. It amended FASB *Accounting Standards Codification™* (ASC) 740, *Income Taxes*, and retained the disclosure requirement in FASB ASC 740-10-50-15(e), which requires a description of tax years that remain subject to examination by major tax jurisdictions. Unfortunately, FASB ASC 740-10-50-15(e) does not specify that unrecognized tax benefits need to exist for the disclosure requirement to apply. As a result, differences of opinion arose despite the fact that paragraphs BC 13-14 in the Basis for Conclusions of ASU 2009-06 are sufficiently clear that entities without material unrecognized tax benefits are not required to disclose tax years open to examination. TPA 5250.15 was in conflict with paragraphs BC 13-14.

Although FASB was aware of the conflict between the TPA and the Basis for Conclusions of ASU 2009-06, the board and staff did not realize that the TPA was causing issues in practice until the CPEA brought the controversy to light. The practice issues became an agenda topic at the February 13, 2015 meeting of the Private Company Council, where the AICPA and FASB staffs promised to work together to reach a solution. This cooperative effort led to the elimination of the TPA. The requirement to disclose a description of tax years that remain subject to examination will be necessary only when an entity has material unrecognized tax benefits.

The clarification and resolution of this issue will be welcome news to many practitioners since the conflicting guidance on disclosing open tax years had caused considerable confusion and controversy, including numerous Matters for Further Consideration and Findings for Further Consideration (FFCs) in peer review. The elimination of the TPA may render moot FFCs on this issue that a firm would ordinarily need to consider in future peer reviews. To that end, the May 2015 Peer Review Update includes revisions to certain checklist questions in the *Peer Review Program Manual* to reflect the rescission of the TPA. Practitioners also should be aware that it may take time to update AICPA accounting and auditing guides to reflect the elimination of TPA 5250.15. The CPEA and TIC will continue to monitor and report on further developments in this area, as well as other practice issues. Visit the CPEA site for more information about its work. ■

Long-Awaited FASB ED Released on Not-for-Profit Financial Statements

A proposed FASB ASU that is intended to improve the information provided in not-for-profit financial statements, including the related notes, would result in significant changes to current practice. The long-awaited ED, *Presentation of Financial Statements of Not-for-Profit Entities*, sets forth the FASB's proposed improvements to current net asset classification requirements and information presented in financial statements and notes to financial statements about a not-for-profit organization's liquidity, financial performance, and cash flows. The proposed ASU, a *FASB in Focus* overview, and two Q&A documents are available www.fasb.org. Comments are due by August 20. ■

GASB Issues Final Statement on Fair Value Measurement and Application

GASB Statement No. 72, *Fair Value Measurement and Application*, defines fair value and describes how it should be measured, specifies that investments should be measured at fair value, and enumerates the information about fair value that should be disclosed in the notes to the financial statements.

The statement defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Investments, which generally are measured at fair value, are defined as a security or other asset that governments hold primarily for the purpose of income or profit and the present service capacity of which are based solely on their ability to generate cash or to be sold to generate cash.

The full text of Statement No. 72 and a GASB In Focus on fair value are available on the GASB website, www.gasb.org. ■

TIC Offers Ideas on GASB Projects

TIC members work behind the scenes to monitor issues that will affect private companies, not-for-profit organizations, and governmental entities and the CPAs who serve them and to speak out on behalf of that constituency. As part of that effort, TIC member Ted Williamson recently attended a GASB public hearing to offer perspective on TIC comment letters on two important GASB preliminary views documents and to gather insights into the board's thinking on these projects. Below are Ted's observations in his own words:

Leases: In TIC's comment letters on this document, our concerns revolved around the cost and effort for governments implementing the guidance versus the value of the results for users. Among its concerns, TIC focused on the GASB's preliminary view that a contract with both lease and service components generally should be separated so that each component is accounted for on its own. TIC believes this would be acceptable only if the lease and service components could be clearly identified and quantified. Although the PV contained an exception to this requirement, TIC thought the conditions for meeting it would add unnecessary cost and complexity. TIC also asked for further guidance on disclosures, because of the potential complexity involved, and asked the GASB to exclude short-term lease disclosures. TIC challenged the GASB's position that a lease with a bargain purchase option must be accounted for as a financed purchase, because in practice governments do not always exercise bargain purchase options. To give governments time to implement the changes and educate grant funders about them, TIC requested a long implementation period. We also asked the GASB to clarify the reasons for differences between its guidance and the elements of the FASB lease project. Since many governments have hundreds of leases, streamlining and minimization of complexity are paramount.

Other hearing participants echoed TIC's concerns about the potential cost and complexity. In their response to comments from TIC and other hearing participants, the GASB representatives questioned the necessity of reconciling their requirements with those of the FASB.

Financial Reporting for Fiduciary Responsibilities: For this PV, the comments generally revolved around the need to make the proposed guidance easier to understand, since it is quite technical. In its comment letter, for example, TIC asked the GASB to further clarify the portions of the PV that indicate what types of activities are included within the scope of the standard, since these are hard to navigate currently. Additionally, TIC had raised issues about scope and the definition of the word "citizenry," since its meaning is important in interpreting the guidance. TIC made recommendations to clarify or improve the tables and charts in the PV. TIC also discussed situations that the document didn't address, such as the treatment of some student activity fees or whether a government that's part of a joint venture with another government has a fiduciary responsibility when it manages the books for the joint venture. TIC also challenged the necessity of the flows statement and presentation of net position for the new custodial fund, since financial statement readers may believe the government has discretion over that money. Some hearing participants suggested agency funds should continue to be presented, and that custodial funds only be used for certain activities currently accounted for in funds other than agency funds. The GASB representatives seemed to be open to that idea and to other changes that we may see in the ED.

The GASB representatives were pleased with TIC's participation in the hearing and attending the event was certainly a very rewarding experience for me. TIC will continue to follow these and other GASB projects and to comment and report on what they mean to our constituents. ■

--Ted Williamson, CPA, TIC member and partner, RubinBrown LLP

TIC Cited in AICPA Comments on PCC Review

TIC was mentioned in a letter from the AICPA responding to the Financial Accounting Foundation's request for comment on a three-year review of the Private Company Council. AICPA President and CEO Barry Melancon and AICPA Board Chair Tommye Barie noted that TIC would be happy to serve as a resource in the PCC's outreach activities. Among other comments, the letter also recommended that the PCC should be a partner to the FASB rather than an advisory board, that the FASB and PCC focus on additional work needed on existing GAAP, that discussions avoid unnecessary complexities and that incoming FAF trustees assigned to the private company initiative and PCC chairs maintain the high standards set by the incumbents. ■

TIC Members' Articles Examine Group Audit Standard

"How Coordination Enables Compliance with the Group Audits Standard," written by TIC member Michael A. Westervelt, is the third in a series of *Journal of Accountancy* articles explaining the application of the standard. The first article, "The Scoop on Group Audits: You May Have Them, Even Though You Think You Don't," was written by Westervelt and the second, "Qualitative Considerations for Allocating Materiality to Components in a Group Audit," was written by TIC member Daniel Sanders. ■

Auditing and Attest News

- The ASB has issued attestation interpretation No. 1 of AT section 201, *Agreed-Upon Procedures Engagements*, to provide guidance for third-party due diligence services performed as agreed-upon procedures engagements related to asset-backed securitizations, as defined in the SEC Release No. 34-72936, *Nationally Recognized Statistical Rating Organizations*. The interpretation addresses:
  - The distribution of procedures or findings, or both, under AT section 201 when due diligence services in the *Form ABS Due Diligence-15E* and *Form ABS-15G*, as applicable, are performed as an AUP engagement;
  - The practitioner's *Form ABS Due Diligence-15E* reporting responsibilities; and
  - How the practitioner might modify the illustrative report wording in AT section 201 to clarify the requirements and limitations of AUP engagements and reports as it relates to due diligence services.

  Notably, the distribution of the procedures or findings, or both, of the practitioner's due diligence services in the *Form ABS Due Diligence-15E* or *Form ABS-15G* is not prohibited because regulations require that the distribution of that information be made available to the public.

- The AICPA has issued Questions and Answers (Q&A) section 9540.01–.05 to provide nonauthoritative guidance to practitioners in connection with American Land Title Association (ALTA) Best Practices Framework. The Q&As address the types of engagements a practitioner may perform, the applicability to an attest engagement, the suitability of criteria, the nature of examination or review procedures, and the form and content of the report. Q&A section 9540.05 also includes illustrative reports. The ALTA Best Practices Framework assists lenders in satisfying their responsibility to manage third party vendors. ■

Accounting Update

- In considering proposed FASB ASU, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date*, TIC approved of the one-year delay of the effective date. TIC did not object to an additional proposal that would allow a two-year transition for retrospectively restating all prior periods presented, but TIC did indicate that adoption of full retrospective presentations by most private entities within TIC's constituency would be unlikely.

- TIC recently issued a supportive comment letter on three proposed Accounting Standards Updates: *Plan Accounting (Topics 960, 962, and 965)—(I) Fully Benefit-Responsive Investment Contracts, (II) Plan Investment Disclosures, and (III) Measurement Date Practical Expedient* (a consensus of the FASB Emerging Issues Task Force).

- FASB recently issued the following EDs for public comment as part of its simplification project:
  - *Business Combinations (Topic 805): Simplifying the Accounting for Measurement-Period Adjustments*
  - *Equity Method and Joint Ventures (Topic 323): Simplifying the Equity Method of Accounting*
  - *Compensation—Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting*

  The comment deadline for the first ED has passed, but the deadline for the second one is August 4 and for the third it is August 14. TIC will be reporting its comments on these proposals in a future *TIC Alert*.

- TIC regularly monitors and comments on standards in development. Newly issued FASB ASUs that TIC had commented on in the ED stage include:
  - FASB ASU No. 2015-01--*Income Statement—Extraordinary and Unusual Items (Subtopic 225-20): Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items*
  - FASB ASU No 2015-02--*Consolidation (Topic 810): Amendments to the Consolidation Analysis* (formerly known as *Consolidation: Principal versus Agent Analysis*)
  - FASB ASU No. 2015-03—*Interest—Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs.*
  - FASB ASU No. 2015-04—*Compensation—Retirement Benefits (Topic 715): Practical Expedient for the Measurement Date of an Employer's Defined Benefit Obligation and Plan Assets*
  - FASB ASU No. 2015-05—*Intangibles—Goodwill and Other—Internal-Use Software (Subtopic 350-40): Customer's Accounting for Fees Paid in a Cloud Computing Arrangement*
  - FASB ASU No. 2015-07—*Fair Value Measurement (Topic 820): Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent) (a consensus of the FASB Emerging Issues Task Force)* ■

Ethics Update

- A PEEC ED on *Firm Mergers and Acquisitions*, addresses two types of relationships with respect to an attest client (that is, employment or association with an attest client and the performance of prohibited nonattest services) that may create independence issues when CPA firms are parties to a merger or acquisition. TIC fully supported the provisions of the proposed interpretation regarding employment or association with an attest client but recommended revisions to the nonattest services section of the proposal to reduce complexity and improve clarity. Among its other comments, TIC also called for adequate time for firms to update systems to address new guidance and recommended that PEEC conduct a robust education campaign.
- Recently issued PEEC documents include:
  - A revised interpretation on "Individual in a Campaign Treasurer or Similar Financial Position"
  - A proposed, revised interpretation that amends the definition of client affiliates
  - A new interpretation, "Breach of an Independence Interpretation" ■

Demystifying the Comment Letter Process for NFPs

On April 22, the FASB issued an ED of a proposed Accounting Standards Update that would significantly change the existing not-for-profit financial reporting model. This article demystifies the prospect of writing a comment letter for financial professionals in not-for-profit organizations. Comments are due by August 20. ■

Exhibit Added Into AU-C Section 501

Exhibit C, "Statement on Updates to Audit Response Letters" in AU-C section 501, *Audit Evidence — Specific Considerations for Selected Items* (AICPA, *Professional Standards*), has been added to include the Statement that the Audit Responses Committee of the American Bar Association published in the Spring 2015 edition of The Business Lawyer. To enhance lawyers' ability to respond efficiently to update requests by auditors—thereby facilitating the audit process and contributing to audit quality—the Statement provides a framework under which a lawyer may furnish an update letter to the auditor, and is helpful in obtaining an update response from a lawyer when considered necessary by the auditor. ■

Let Us Hear From You

If you have questions, local firm advocacy issues or suggestions for TIC, contact:

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