

**Blue-Ribbon Panel on Standard Setting
for Private Companies**

**Report to the Board of Trustees of the
Financial Accounting Foundation**

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BLUE-RIBBON PANEL (BRP) ON STANDARD SETTING FOR PRIVATE COMPANIES

I. EXECUTIVE SUMMARY

In December 2009, the American Institute of Certified Public Accountants (AICPA), the Financial Accounting Foundation (FAF), the parent organization of the Financial Accounting Standards Board (FASB), and the National Association of State Boards of Accountancy (NASBA) established a “blue-ribbon” panel (the Panel or BRP) to address how accounting standards can best meet the needs of users of U.S. private company financial statements.¹ The Panel was charged with providing recommendations on the future of standard setting for private companies to the FAF Board of Trustees (the Trustees). (See Appendices A and B for additional information about the Panel and the conduct of its work.) This report represents the culmination of the Panel’s work and includes its members’ recommendations to the Trustees.²

The Panel has concluded that there are urgent and growing systemic issues that need to be addressed in the current system of U.S. accounting standard setting. The Panel members believe that the system has not done a sufficient job of (a) understanding the information that users of private company financial statements consider decision-useful and how those information needs differ from those of users of public company financial statements and of (b) weighing the costs and benefits of GAAP for use in private company financial reporting. These issues have caused a lack of relevance of a number of accounting standards for many users of private company financial statements and an overall level of complexity in U.S. GAAP that continues to concern preparers of private company financial statements and their CPA practitioners. Some members believe that GAAP is overly complex for public companies, too. Many Panel members believe that within the U.S. marketplace, significant, unnecessary cost is being incurred for GAAP financial statement preparation and audit, review, or compilation services. Thus, change is urgently needed.

This report proposes major and other enhancements aimed at fostering an accounting standard-setting system that would seek to maintain a high degree of financial reporting comparability for business entities, regardless of capital structure, but also significantly increase the chances of effecting potential differences, where warranted, in measurement, recognition, and presentation, and not just disclosure. The Panel believes that, at least in the near term, the system should focus on making exceptions and modifications to U.S. GAAP for private companies that better respond to the needs of the private company sector rather than move toward a separate, self-contained GAAP for private companies or a wholesale reorganization of GAAP.

¹While some stakeholders had suggested that the Panel’s work include private-sector not-for-profit entities (NPEs) as well, the Panel has limited its work to private for-profit companies. The Panel acknowledges that many NPEs have a much broader and somewhat different set of users of their GAAP financial statements, either directly or indirectly (through the IRS’s Form 990), than do many private companies.

²As noted in Appendix A, the Panel or BRP comprises 18 members (including 1 nonvoting member) but also benefited from input from several nonvoting participating observers. References in this report to Panel conclusions and recommendations should be interpreted as those of its voting members rather than its participating observers. The BRP acknowledges that on January 14, 2011, the FAF announced the appointment of Daryl Buck to the FASB for a term beginning February 28, 2011. In light of this announcement, Mr. Buck resigned as a member of the BRP on January 17, 2011, and did not participate in the final vote.

One major enhancement, supported by a supermajority of Panel members, is to establish, under the FAF's oversight, a separate private company standards board to help ensure that appropriate and sufficient exceptions and modifications are made, for both new and existing standards. That new board would work closely with the FASB to achieve a coordinated and efficient standard-setting process but would have final authority over such exceptions and modifications. A comprehensive review of the new board would be conducted in three-to-five years to evaluate its effectiveness and determine whether to maintain it as is, make additional process improvements, or sunset it.

Another major enhancement, supported by all Panel members, is to create a differential framework (set of decision criteria) to facilitate a standard setter's ability to make appropriate, justifiable exceptions and modifications.

The Panel is also recommending certain short-term and transitional actions by the FAF and the FASB to provide near-term relief for private companies and help ensure a smooth transition to a new board.

These recommendations were developed after examining a full range of options that included everything from maintaining the status quo to developing an entire new set of standards for private companies. In making the recommendation for a new board, the Panel has considered the actions currently under way by the FASB to help improve the standard-setting process for private companies (including those described in Appendix F), along with the recommended short-term and transitional actions. A supermajority of the Panel believes that these actions do not remove the need or the urgency for a new standards board for private companies.

Section II of this report contains the Panel's principal recommendations of a U.S. GAAP model with exceptions and modifications for private companies and a separate private company accounting standards board to set those exceptions and modifications. Section III describes the problems that the Panel has identified in the current standard-setting system. Section IV describes why the Panel believes its recommendations will best address the problems identified. Section V contains the recommendations that the Panel believes are important in helping transition to and otherwise achieving the recommended model and structure. Section VI captures alternative views held by a small minority of the Panel members.

We urge the Trustees of the FAF to consider carefully and act upon each of the recommendations of the BRP, and we thank the FAF, the AICPA, and the NASBA for requesting us to consider this important issue.

II. BRP RECOMMENDATIONS ON STANDARD-SETTING MODEL AND STRUCTURE

- **GAAP with exceptions and modifications for private companies (with process enhancements)**
- **Separate private company accounting standards board**

The BRP recommends a U.S. GAAP model with exceptions and modifications for private companies, with process enhancements. A supermajority of BRP members further recommend that a separate private company standard-setting board under the FAF be established to ensure that those enhancements are made and result in appropriate and sufficient exceptions and modifications for private companies.

A. RECOMMENDED MODEL

U.S. GAAP with Exceptions and Modifications for Private Companies (with Process Enhancements)

The BRP recommends that accounting standards for private companies be based on existing U.S. GAAP (The *FASB Accounting Standards Codification*TM) but with exceptions and modifications that would result in financial statements that provide relevant, decision-useful information that meets the needs of users of private company financial statements in a cost-effective manner. Private company accounting standards under this model would be based on existing U.S. GAAP modified as necessary in the standard-setting process. This model contemplates the continued use of U.S. GAAP for public and private companies, with exceptions and modifications made for private companies. The BRP believes that appropriate modifications and exceptions to existing GAAP should be made to better meet the needs of users of private company financial information. This could result in different measurement, disclosure, presentation, and recognition standards for private companies, but the modifications and exceptions would have to be justified using a differential framework (set of decision criteria) and not created just for the sake of having differences.

A cost-benefit analysis would be performed to take into account the costs to prepare, report on, and use the financial statements. The benefit side of the equation would consider whether or not users would be able to make appropriate decisions with the information provided and whether those users have access to management to obtain additional information. In other words, is the information in the financial statements relevant and necessary, and can additional information be made available to such users, if needed? The BRP understands that the cost-benefit analysis can sometimes be subjective in nature because of the difficulty in estimating the monetary consequences of omitting information in the financial statements or having one measurement attribute versus another.

Another important aspect of the BRP recommendations is the creation of a differential framework to enable the private company accounting standard-setting board to evaluate whether exceptions or modifications are needed for private companies. The BRP envisions the framework

functioning as a guide to evaluate whether differences would be appropriate, rather than as an entirely new foundation from which to develop a separate body of GAAP for private companies. The BRP considers this framework, and the willingness to interpret the framework to create differences, to be essential to the successful implementation of this model. Historically, standards have been established with differential reporting for private companies without defining what should constitute a difference. This lack of a differential framework has contributed to the current private company concerns about relevance, complexity, and costs.

B. RECOMMENDED STRUCTURE

Separate Private Company Accounting Standards Board

To complement the model, a supermajority of BRP members recommend that the FAF create a separate accounting standards board (hereinafter referred to as “new board”) with the ultimate standard-setting authority to determine and set exceptions and modifications in GAAP for private companies. The paragraphs below highlight some of the key features that the Panel recommends for the new board. Additional detail is provided in the chart in Appendix C.

New Board Mission and Process

As stated earlier, the new board’s mission would be to establish appropriate exceptions and modifications to GAAP for private companies, while helping to ensure that users of private company financial reports receive decision-useful information. The new board would monitor the activities and deliberations of the FASB and work alongside the FASB as necessary to ensure that differences in GAAP for private companies, where warranted, are promulgated efficiently and effectively. The BRP believes the FASB, working with the new board, should try to develop the best possible standards for all entities. The differential framework, as discussed above, will help in determining whether differences in GAAP for private companies are warranted.

Either the new board or the FASB could promulgate differences depending on the circumstances of the topic. However, the Panel members believe it is critical that all differences reside in the one GAAP codification. For example, the FASB likely would not attempt to promulgate a difference on an existing GAAP standard that is not on its project agenda, and thus the task would be handled by the new board, which would initiate its own project. If a topic is on the FASB’s agenda, the FASB might promulgate a difference (with the support of the new board) or the new board might promulgate a difference if the FASB believes such a difference is unwarranted.

Regardless of how the boards choose to operationalize the promulgation of differences on a facts-and-circumstances basis, the Panel believes that the ultimate authority to approve the exceptions and modifications should reside with the new board. The new board could also initiate its own projects as deemed necessary.

Other Specifics on Board Recommendation

The new board would consist of members that are representative of the private company sector and would work closely with the FASB. The new board would have the responsibility to

conduct outreach to private company stakeholders and provide input and feedback to the FASB. Nothing would preclude the FASB from receiving input from private companies, but the specific responsibility for seeking such input would reside with the new board. The FASB and new board would each have official observers at their respective meetings to maintain effective two-way communication. (The FAF could further solidify this coordination by having the primary advisory board to the new board also advise the FASB on private company matters.) Much of the cost for the new board and staff would likely require funding by a viable, new source, such as mandatory annual or one-time (endowment) contributions from stakeholders.

Comprehensive Review of the New Board

The BRP believes that the FAF's oversight and governance should include a comprehensive review of the new board after three-to-five years. This comprehensive review should evaluate the effectiveness of the board and determine whether to maintain the board as is, make additional process improvements, or sunset the board. The FAF's review should include but not be limited to the following qualitative and quantitative measures:

- A survey to collect qualitative information from private-company-sector stakeholders, such as, but not limited to, financial statement users' concerns about relevance and complexity and preparers' and practitioners' concerns about complexity and cost-benefit. A baseline survey could be taken in the near future, and subsequent surveys would be compared with the results of the baseline survey.
- To the extent the information can be obtained, obtain quantitative information on the prevalence of (1) audit/review/compilation reports with GAAP exceptions and (2) Other Comprehensive Basis of Accounting (OCBOA) financial statements. Information obtained in subsequent years would then be compared to such baseline information.

Additionally, the BRP believes that the FAF's recently initiated post-implementation assessment of FASB and GASB standards also should apply to significant differences in GAAP that the new board may approve for private companies. Such reviews would be crucial in assessing how well the two-board system is functioning and also help assist the FAF in determining the next stage of evolution in standard setting for private companies as described below.

The BRP believes that the recommendations on the model and structure described above are the best solution to the problems in the current standard-setting system for private companies that are discussed in the following section. Section IV of the report provides the BRP's primary reasons for this belief.

III. WHAT THE RECOMMENDATIONS ARE ADDRESSING—THE PROBLEM STATEMENT

There are approximately 28 million private companies in the United States.³ Many are very small businesses that have no reporting requirements other than filing income tax returns. However, a significant number of private companies are required to prepare GAAP financial statements by lenders, bonding companies, regulators, and others, in addition to the approximately 14,000 public companies, which have SEC reporting requirements. Most of the private companies preparing GAAP financial statements do not have the accounting resources that public companies have, especially larger public companies.

The BRP has concluded that the current U.S. accounting standard-setting process has systemic issues, involving (a) an insufficient understanding of the needs of users of private company financial statements and (b) an insufficient weighing of the costs and benefits of GAAP for use in private company financial reporting. These issues have caused a lack of relevance of a number of accounting standards—for example, those on variable interest entities, uncertain tax positions, fair value measurements, and goodwill impairment—for many users of private company financial statements. Since it also appears that the least relevant standards for private company users are often the most complex, the BRP believes that private companies are incurring significant unnecessary cost for GAAP financial statement preparation and audit, review, or compilation services. Indeed, the increase in costs to provide potentially irrelevant information has led to more users who are willing to accept qualified opinions—a development that calls into question whether those aspects of GAAP are truly “generally accepted.” These increasing instances of nonacceptance, coupled with a concern about the overall complexity of GAAP expressed by many private company preparers and their CPA practitioners—a concern that some BRP members have noted extends to public companies as well—have led the BRP to conclude that, at a minimum, the current accounting standard-setting system needs to be improved to better address the needs of users of private company financial statements in a cost-effective manner.

Based on both the FASB’s history and the competing standard-setting pressures on the FASB that are emanating from the public company sector, including those related to the FASB’s joint projects with the International Accounting Standards Board (IASB), a supermajority of BRP members believe that the FASB will not be able to fully assess and respond sufficiently and appropriately to the needs of the private company sector.

In arriving at these conclusions, the BRP has considered:

- Previous studies

³This number is based on the U.S. Census Bureau’s *Nonemployer Statistics: 2008* report (21.4 million nonemployer establishments) and *2008 County Business Patterns* report (7.0 million employer establishments, excluding not-for-profit and government establishments, and the approximately 14,000 public companies). Only businesses that are subject to federal income tax are included in the *Nonemployer Statistics: 2008* report. Accordingly, most not-for-profit entities are excluded from that figure, except those that are not exempt from federal income tax.

- The experience of the Private Company Financial Reporting Committee (PCFRC), as described primarily by the current PCFRC chair and a former PCFRC member, who serve as a participating observer and a BRP member,⁴ respectively
- The FASB's activities historically
- The growing use of reports with GAAP exceptions and the availability of IFRS for Small and Medium-sized Entities (SMEs)
- Individual BRP members' perspectives (generally representing their constituent organizations) about the current system
- Feedback received through written public submissions
- The experience of international standard setters who have addressed similar issues.

PREVIOUS STUDIES

BRP members were given an overview of the numerous studies, reports, and recommendations on private company accounting that have been prepared over the last 40 years. (A full list of those studies and reports is contained in Appendix D.) Most of the older studies were practitioner-driven. The last time that the FASB formally researched the needs of private companies was in 1983. Since that time, the number of standards that have been issued by the FASB (now included in the Accounting Standards Codification) has increased greatly. Some private company constituencies have said that some of the more recently issued standards have shown little to no relevance to their users coupled with an overall increase in complexity of those standards. Two of the more noteworthy reports were the Wheat and Castellano Reports.

The Wheat and Castellano Reports, Conclusions, and Associated Activities

In 1971, the AICPA conducted a study (Study) that had a significant effect on the standard-setting process in the United States and produced what was called the Wheat Report. The Study was charged with examining the process and means by which accounting principles were established in the United States and providing recommendations for improvement. At that time, accounting standards were being established by the Accounting Principles Board (APB), a senior committee within the AICPA. The Study recommended the creation of the FAF and the FASB. The FAF would oversee the FASB, hence replacing the APB. The FASB would be an independent body with a full-time board and research staff. The Study reached this conclusion after reviewing and addressing the independence of the current APB board and the benefits and costs of having a part-time board. (Appendix E provides current information about how the FASB is constituted, operates, and is overseen by the FAF.)

After the creation of the FASB, there were a number of other studies (as listed in Appendix D) conducted that were generally focused in part on what the accounting profession calls "standards overload." The most recent study on private company accounting was done in 2005 by an AICPA task force, which produced what is referred to as the Castellano Report.

⁴Daryl Buck was a PCFRC member from 2007 to 2009. The BRP acknowledges that on January 14, 2011, the FAF announced the appointment of Mr. Buck to the FASB for a term beginning February 28, 2011. In light of this announcement, Mr. Buck resigned as a member of the BRP on January 17, 2011, and did not participate in the final vote.

The AICPA formed the Private Company Financial Reporting Task Force (the Task Force) to conduct research to determine whether private company GAAP financial statements were meeting the needs of their users and whether the cost of providing GAAP financial statements was justified compared to the benefits of doing so. On the basis of the research performed, the Task Force concluded that the users of private company financial statements have different needs than users of public company financial statements, that GAAP exceptions and OCBOA should not be the resolution to the private company financial reporting problems, and that fundamental changes should be made to the current standard-setting process.

The Castellano Report was presented to the FAF Trustees in 2006. The FASB responded by issuing an Invitation to Comment, *Enhancing the Financial Accounting and Reporting Standard Setting for Private Companies*, and subsequently forming the PCFRC in 2007 and adding a staff member with extensive experience in the private company sector. That individual's role was to work with the PCFRC, otherwise liaise with the sector, educate the FASB Board and staff about private company issues, and offer alternatives for private companies during the standard-setting process.⁵

Because of the extensiveness of the research conducted in connection with the Castellano Report, and because the BRP's ensuing discussions and the responses contained in the written public submissions were generally consistent with the Castellano Report's findings, most BRP members do not believe that additional formal research is needed at this time.

THE PCFRC AND FASB ACTIVITIES SINCE 2007

The PCFRC began its work in 2007. By its charter, the PCFRC consists of a chair who is a part-time employee of the FASB, four users of private company financial statements (currently two commercial bank lenders, a surety, and a venture capitalist), four preparers of private company financial statements (current members represent companies with annual revenues ranging from \$25 million to \$1 billion), and four CPA practitioners (who have been from small to mid-size firms). Since very small private companies generally rely on their CPA firms to assist with the preparation of financial statements in accordance with GAAP, the CPA practitioners are seen as representing the smaller companies.

⁵These changes built upon the FASB's creation of a Small Business Advisory Committee (SBAC) in 2004. Stakeholders viewed the SBAC as an important step forward in the standard-setting process, helping to put the Board more in touch with the concerns of smaller businesses, both public and private. However, some stakeholders also felt that the SBAC did not provide sufficient input for the Board to comprehensively address private company concerns.

Over the years, the SBAC has played a valuable role in providing strategic and other advice to the FASB about its standard-setting process and proposed and existing standards, as they pertain to small businesses, both public and private. In discussing standard setting for private companies, its members have noted that the informational needs of private company users are often different from those of public company investors and that those differences should be considered by the FASB throughout its projects. Its members have also called upon the FASB to continue to improve the Board's outreach to the private company sector throughout the standard-setting process.

The PCFRC's mission is to provide recommendations that will help the Board determine whether there should be differences in prospective and existing accounting standards for private companies. The PCFRC meets four to five times per year to evaluate existing and proposed standards from a private company perspective to develop positions for their recommendation letters. Consistent with the FASB's open due process, the PCFRC's meetings are open to the public. Beginning in April 2010, Board members began attending the PCFRC meetings on a rotating basis, allowing for better two-way communication.

The FASB addresses the PCFRC's recommendations and is supposed to articulate within the basis for conclusions section of standard-setting documents (both Exposure Drafts and final Accounting Standards Updates) the basis for its decisions on whether differences should exist for private companies.⁶ Although the Board considers the recommendations received from the PCFRC, it has not always documented in the basis for conclusions why it did not agree with the PCFRC's recommendations.

Over time, internal changes have been made at the FASB to better focus on private company issues. In June 2009, an assistant staff director was named to oversee all nonpublic entity (private company and not-for-profit organization) issues. The BRP also notes that all recent Exposure Drafts have directly posed questions about how a proposed standard would affect nonpublic entities.⁷

The PCFRC has submitted approximately 40 recommendation letters since its formation in 2007. The Board, considering PCFRC input along with input from other sources, has made various modifications to standards, generally involving different effective dates for private companies and in some cases different disclosures. These changes notwithstanding, the PCFRC chair has indicated that many stakeholders in the private company sector have seen the PCFRC's work with the FASB as not being wholly successful because the FASB has not also shown a willingness to consider carefully and approve, where appropriate, the possibility of measurement, recognition, or presentation differences. (This message was echoed in the written public submissions.)

GROWING USE OF REPORTS WITH GAAP EXCEPTIONS AND AVAILABILITY OF IFRS FOR SMEs

Unlike other countries around the world, the United States has no statutory requirement for private companies, other than certain regulated companies such as financial institutions,⁸ to prepare GAAP financial statements. Under current practice in the United States, private companies may report under U.S. GAAP or OCBOA (usually cash or income tax basis). Because the AICPA now recognizes the IASB as an authoritative standard setter, in many instances private companies (other than financial institutions) may also report under IFRS or IFRS for

⁶This requirement was articulated in the Invitation to Comment that preceded the PCFRC's formation (see p. 8).

⁷In recent months, the FASB has continued to make various changes to its processes concerning nonpublic entities, including transferring additional staff to specifically work in that area. These changes are described in Appendix F.

⁸Federal law requires accounting principles applicable to reports or statements required to be filed with the federal financial institution regulators by insured depository institutions and credit unions to be uniform and consistent with GAAP.

SMEs,⁹ although thus far there do not appear to be many private companies that have chosen this option.

Because of the lack of relevance, and the complexity, surrounding some GAAP standards, notably accounting for variable interest entities (formerly FASB Interpretation No. 46(R), *Consolidation of Variable Interest Entities*, as recently amended by FASB Statement No. 167, *Amendments to FASB Interpretation No. 46(R)*), many private companies have opted to receive qualified or except-for opinions. Lender and CPA-practitioner members of the BRP have reported that they have seen an increase in the acceptance of such reports from private companies, mainly because application of some standards does not produce relevant information for lenders and is costly to prepare and audit, review, or compile. Some would respond that this is not necessarily a problem, as users of private company financial statements accept them. However, it does raise concerns about potentially reaching a point at which the frequency of exceptions undermines the very idea of “generally accepted.” In addition, many loan covenants for larger private companies require GAAP financial statements and these companies typically do not have the option of taking exceptions or using OCBOA.

INDIVIDUAL BRP MEMBER PERSPECTIVES

At its first meeting, the BRP heard from its members who are users of private company financial statements. Users of private company financial statements primarily include lenders, other creditors, bonding and credit-rating agencies, regulators, and business owners. While the specific informational needs varied among users, they told the BRP that they liked the “gold standard” of GAAP, for consistency, comparability, and related assurance. According to these members, most users focus heavily on cash flow measures, adjust the financial statements to meet their end needs, and do not make decisions on the basis of the financial statements alone. Users almost always require additional information when making decisions to lend, invest, or bond, and many users have access to management to obtain that information. (This contrasts to the lack of direct access to management for certain users of public company financial statements under the SEC’s Regulation FD.) These members stated that certain GAAP standards are complex, and that most companies, especially smaller ones, need outside CPA assistance to comply. They also noted that more recently, companies seem to be taking more exceptions to GAAP because certain information is not relevant. These users stated that while comparability is certainly important to them, they would not oppose differences in GAAP for private companies, perhaps even a separate standalone set of U.S. GAAP along the lines of IFRS for SMEs or Canadian GAAP for Private Enterprises, if that would spur more companies to move from OCBOA to GAAP financial statements. However, some BRP members observed that the call for change did not seem to be coming, in any widespread way, from the user community and that the users of private company financial statements are accustomed to adjusting financial statements to make the financial statements more useful for their end needs.

At the second meeting, preparers and practitioners agreed that there are broad-based concerns about the current standard-setting system. They stated that private company issues have not been

⁹IFRS for SMEs specifically preclude all financial institutions, including those that are privately held, from using these standards.

heard or fully considered by the FASB, and that the FASB has not made sufficient exceptions or modifications for private companies in measurement and recognition, as well as disclosure. As a result, those preparers and practitioners indicated that standard setting seems to be driven to a large degree by public company financial statement user needs and often tends to be more relevant to some of the users in that sector (especially equity investors) than it does to many users in the private company sector.

At later meetings of the BRP, the word *relevance* was frequently used when speaking about accounting standards. Most BRP members agreed that too many GAAP requirements were not relevant to some users of private company financial statements and that the benefits of complying with certain standards did not justify the costs. The BRP noted that change would not be driven by private company financial statement users. Rather, the users would likely accept differences in GAAP for private companies, since some GAAP pronouncements are not useful or relevant to providing appropriate understanding or analysis of the entity's relative financial position.

FEEDBACK FROM PUBLIC SUBMISSIONS

The BRP published a set of questions on August 5, 2010, requesting written input from the public. Appendix G to this report contains the questions asked, a list of respondents, and a full summary of the responses received. Many CPA practitioners and preparers responded but few users submitted responses.

The common issues and concerns cited by respondents were:

- Private company financial statements often lack relevance to users.
- Standards have become increasingly complex.
- The pace of the standard-setting process has increased.
- Costs often exceed benefits.
- There has been an increase in qualified opinions and use of OCBOA where possible.

The general thrust of the written responses did not differ from the general thrust of comments made by most BRP members, with many respondents indicating that there were systemic issues with the standard-setting process. The largest firms, however, generally recommended attacking the issue of complexity through simplification efforts for all entities, both public and private, especially until the SEC makes a decision about whether to incorporate IFRS into the financial reporting system for public companies. While supporting one set of high-quality standards for all public and private companies in the United States, the Federal financial institution regulators¹⁰ recognized that accounting standards need to address the circumstances and needs of all financial statements users, for both public and private companies. In their written response to the Panel, the regulators recommended that the standard setters include more small-firm and private company representation on a single board and incorporate practical expedients, wherever

¹⁰The U.S. federal financial institution regulatory agencies as a group is a participating observer on the Panel, but is not a member of the Panel.

possible, that would allow the standards to be implemented by all companies in a cost-effective manner.

THE INTERNATIONAL EXPERIENCE

The Panel consulted standard setters outside the United States to learn what is being done for private companies as their public companies adopt IFRS. Most standard setters have come to believe that one size does not fit all when it comes to accounting standards and that there needs to be significant differences for private company reporting:

- A number of countries around the world have adopted IFRS for SMEs. Most of these countries have universal or widespread statutory reporting requirements for all companies, public and private, which in part drove the initiative for the SME project.
- The U.K. is planning to adopt IFRS for SMEs for use by its private companies and, for now, to continue to allow very small private companies to use its Financial Reporting Standard for Smaller Entities (FRSSE) standards.
- Canada has taken a “made in Canada” approach by simplifying existing Canadian GAAP and creating a standalone set of accounting standards for private enterprises. It has an advisory board to the Canadian Accounting Standards Board, which will propose updates and changes, but the ultimate authority to change accounting standards for private enterprises remains with the Canadian Accounting Standards Board. Going forward, changes to IFRSs will be examined to determine whether similar changes should also be made to the accounting standards for private enterprises. This does not mean that the private enterprise standards are on a path to converge with IFRSs for SMEs. The private enterprise standards are a long-term solution focused on the needs of the private enterprise marketplace and will exist as long as the marketplace finds them useful.

BRP CONCLUSIONS

After considering prior studies, the PCFRC’s experience, trends in the marketplace, the perspectives of BRP members, the public written submissions, and the experience of international standard setters, the BRP believes that significant change is needed in the system of setting accounting standards for private companies to address the issues underlying the lack of relevance of a number of GAAP standards for many users of private company GAAP financial statements and the complexity of GAAP for private companies. Some of the BRP members acknowledge that some of the complexity concerns extend to public companies and that some of the relevance concerns extend to some users of public company GAAP financial statements; however, the BRP’s focus is on providing recommendations that are within its purview—the accounting standard-setting system as it pertains to private companies. The BRP believes that the recommendations in Sections II and V are in the best interest of users of private company financial statements and will sufficiently address the systemic issues in a cost-effective manner.

IV. WHY THE BRP’S RECOMMENDATIONS BEST ADDRESS THE PROBLEMS

To develop its best recommendations for addressing the systemic issues described in Section III, the BRP considered various models and structures as alternatives to the current standard-setting process. The individual models and structures contemplated what would be in the best interests of the private company sector in the United States, that is, the process and product that would best facilitate financial reporting to meet the needs of users of private company financial statements in a manner that is cost-effective for private company preparers, practitioners, users, and others in the financial system. The models and structures, which are further detailed in Appendix H, describe an end-state process, taking into account that there might be certain short-term and long-term actions that would need to occur to achieve a particular model or structure.

This section provides a brief overview of the models and the structures considered and explains why a U.S. GAAP model with exceptions and modifications for private companies and a separate private company standard-setting board are the best recommendations to address the problems noted in Section III of the report.

OVERVIEW OF MODELS AND STRUCTURES

The BRP initially debated the following models:

U.S. GAAP Models

- **U.S. GAAP with Exceptions and Modifications for Private Companies—current system**
- **U.S. GAAP with Exceptions and Modifications for Private Companies—with process enhancements**
- **Baseline U.S. GAAP with Add-ons for Public Companies**
- **Separate, Standalone U.S. GAAP for Private Companies Derived from Current U.S. GAAP (the “Canadian” Approach)**
- **Separate, Standalone U.S. GAAP for Private Companies Developed from the Ground up Based on Robust Private Company Framework**

IFRS Models

- **IFRS for SMEs as Issued by the IASB**
- **IFRS for SMEs Customized (“Americanized”) for U.S. Private Companies**

These models were viewed as two continua, one based on U.S. GAAP and another based on IFRS. Within each continuum, the change necessary to achieve such models gradually increased with respect to current standards and the standard-setting system. In all the U.S. GAAP-based models except the current system model, the creation of some sort of underlying, standard-setting framework for private companies was viewed as a near-term necessity. The private company framework in the respective models ranged from a differential framework to a separate, ground-up framework. The IFRS-based models already have an underlying set of decision criteria (“Concepts and Pervasive Principles”) created by the IASB.

The Panel rejected four of the models during its initial deliberations:

- U.S. GAAP with Exceptions and Modifications for Private Companies—current system
- Separate, Standalone GAAP for Private Companies Developed from the Ground up Based on Robust Private Company Framework
- IFRS for SMEs as Issued by the IASB
- IFRS for SMEs Customized (“Americanized”) for U.S. Private Companies.

In general, these models were rejected because that BRP felt that:

- The status quo is unacceptable.
- Separate, standalone GAAP created from the ground up could take a significant amount of time to create and could be significantly different from current U.S. GAAP.
- U.S. private companies should not be leading the charge, *en masse*, to an IFRS-based set of standards before the SEC makes a decision on U.S. public companies, especially given the extent of change management efforts that private company stakeholders might have to undertake.

The remaining three models were refined for further deliberations. Two of the models contemplated two structural variations, one featuring a restructured FASB and the other featuring a separate private company board. Because of the nature of the baseline model, only a version with a single standard-setting board for both public and private companies (a restructured FASB) is feasible and was considered.¹¹

The baseline U.S. GAAP with add-ons for public companies and the separate, standalone GAAP for private companies derived from current U.S. GAAP were not supported by the majority of the BRP members. However, most members believed a baseline or a separate private company GAAP (based on current U.S. GAAP) could be in the best, long-term interest of users of U.S. private companies’ financial statements within the broader context of the overall U.S. financial reporting system. Under a baseline GAAP model, the “burden of proof” would shift more to justifying why users of public company financial statements need certain information, rather than why users of private company financial statements do not. And a separate private company GAAP could permit a more exclusive focus on the needs of users of private company financial statements, more than would other models.

There was an overriding concern among BRP members that a baseline GAAP model or a separate private company GAAP model would likely take much longer and be more costly to implement than a GAAP model with exceptions and modifications, with enhancements to the current system. As such, the BRP rejected these models because of expediency. Many users on the BRP also support a GAAP model with exceptions and modifications, with enhancements to the current system, for reasons of consistency and comparability.

¹¹Baseline GAAP with add-ons for public companies contemplates reviewing and reorganizing current (existing) U.S. GAAP into a baseline GAAP for all entities, based on user needs, and with additional GAAP requirements (“add-ons”) for public companies. Having two boards sharing responsibility for determining that baseline was not considered practicable.

PRIMARY REASONS FOR THE BRP RECOMMENDATIONS

As noted above, many of the models had attributes that were attractive to BRP members, but the overriding factors that led the BRP to choose the recommended model from others are a sense of urgency and the support by many users for financial statement comparability. A U.S. GAAP model with exceptions and modifications for private companies affords the best opportunity to implement change quickly and, with proper coordination between the boards, affords relatively less opportunity for unintended divergence to a separate, standalone GAAP, which could result in less comparability and confusion in the marketplace.

Change Needs to Be Made Quickly

As noted above, some models were appealing as long-term solutions, but the BRP believes that those models could not be achieved quickly enough to provide relief to private companies in the near term. For example, some BRP members noted that a model with a baseline GAAP for all companies and additional requirements (“add-ons”) for public companies would be their ideal solution but that the time to develop such a model would be significant and would not provide near-term relief. That model would require an analysis of all GAAP requirements, possibly with significant involvement by the SEC. Such a task would be difficult at best and might have been more appropriate years ago.

Another model that had some appeal to BRP members but that was rejected to achieve a near-term solution was the creation of a separate set of U.S. GAAP for private companies. That solution was viewed by some BRP members as a long-term goal, but it would require much more time to develop because it would involve a similar analysis of all GAAP requirements as would be required to create the baseline GAAP portion of the baseline-with-add-ons model described in the preceding paragraph (though it would probably not necessitate significant SEC involvement).

Those BRP members who perceived other models as potential long-term solutions believe that U.S. GAAP with exceptions and modifications could be a stepping stone or bridge to those ends. They note that the recommended model does not close off the possibility of a strategic shift by the FAF and the standard setter(s) to one of these other models if it is determined, sometime in the future, to be in the best interest of users of private company financial statements and other stakeholders in the U.S. financial reporting system.

Comparability

BRP members that are primarily financial statement users indicated that comparability is an important attribute for them. A GAAP model with exceptions and modifications for private companies would be based on a single foundation or set of core principles. If GAAP for private companies were a separate document created independently from GAAP for public companies, it could result in two GAAPs that might diverge more dramatically than would be desirable, resulting in less comparability and potentially more confusion in the marketplace.

New Board

The supermajority view of BRP members is that the current FASB and even a restructured FASB cannot produce the needed exceptions and modifications to GAAP for private company financial reporting. Those BRP members believe that throughout its history, the FASB has been geared, in its composition and its processes, very heavily toward public companies, with exceptions and modifications in GAAP for private companies too rare and extremely difficult to achieve, especially in areas other than disclosure—that is recognition, measurement, and presentation. Members of a board with authority to set accounting standards for private companies must possess the perspective of those stakeholders, and the FASB cannot be sufficiently restructured or possess enough of the essential private company representation needed to set GAAP for private companies. A new board is the most realistic path forward in overcoming the systemic issue related to the relevance of GAAP for private companies.

PROS AND CONS CONSIDERED FOR THE BRP RECOMMENDATIONS

The BRP considered the following pros and cons in its deliberations to arrive at the recommended model and structure:

Pros:

A GAAP-with-exceptions-and-modifications model:

- Can be achieved more quickly than some of the other models considered
- Maintains a significant degree of consistency and comparability between public and private companies compared with other models considered
- Minimizes the costs to private companies that choose to “go public” compared with other models considered
- Avoids confusion and system complexity from two highly divergent sets of U.S. GAAP
- Has lower education and training costs than other models considered.

A separate private company board:

- Could provide appropriate structural separation from the pressures that the FASB faces in addressing the needs of public company stakeholders, including the SEC
- Could better address the different needs of private company financial statement users given a targeted focus on one constituency.

Cons:

- A GAAP-with-exceptions-and-modifications model might not be perceived as being sufficiently responsive to complexity and cost issues for private companies (compared with, for example, a separate, self-contained set of private company standards).
- Since the pace of standard setting is often driven (or perceived to be driven) by SEC/public company sector needs or concerns, a GAAP-with-exceptions-and-modifications model probably affords less opportunity for the standard setter to keep the pace of standard-setting activities to a level that facilitates participation by the private company

sector (which generally has fewer resources) in the standard setter's due process compared with other models considered.

- Depending on the extent of exceptions and modifications made by the new board, the result could be substantially different accounting standards for private companies resulting in a lack of comparability, and additional costs and strain to some in the U.S. financial reporting chain. Once a separate board is given authority over private company standard setting, there may be limited ability to stop any such divergence.
- Two boards having authoritative responsibility for an overall, single-GAAP model is unproven and has not been used in other countries.
- It could make engagement in due process inefficient and even confusing for stakeholders that are interested in both public and private companies, and it could possibly undermine the authority of one or both boards.
- Additional funding sources will be required.

The BRP considered the various pros and cons and placed more weight on some factors than on others. The general consensus was that although some models had appeal in the long term, the recommended model has the advantage of achieving needed relief in the near term without adding significant complexity or comparability complications. The BRP also believed that, with a clear mission for the new board, proper coordination of the board with the FASB, and appropriate oversight of the board by the FAF, at least some of the cons would be mitigated.

CONCLUSION ON BRP RECOMMENDED MODEL AND STRUCTURE

In light of the frustrations expressed about the lack of relevance of some GAAP standards and the complexity and rapid pace of change in GAAP by many private company preparers and CPA practitioners in the written public submissions and elsewhere, and because of the length of time needed to achieve the various end-state models, the BRP recommends the U.S. GAAP model with exceptions and modifications for private companies, set by a separate private company board. The BRP believes that this model and structure would be the most effective approach to improve relevance of standards and to get relief for private company stakeholders in the near term. The BRP acknowledges that a two-board structure has risks (as noted above) but firmly believes that through proper coordination and effective two-way communication, the two boards will be able to set appropriate standards that best meet the needs of users of private company GAAP financial statements in a cost-effective manner.

The BRP also recognizes that the FAF or the new board could consider a succession (evolution) of models, such as described on page 15, as a longer-term solution.

V. ADDITIONAL BRP RECOMMENDATIONS: SHORT-TERM, TRANSITIONAL, AND OTHER

Short-term and Transitional Actions by the FASB and the FAF

While the BRP firmly believes that significant change is urgently needed and encourages the FAF to take prompt action to implement the Panel's recommendations on model and structure, the Panel recognizes that the Trustees will need time to vet the recommendations, especially concerning the creation of a new board, both internally and publicly, and, if the Trustees concur,

to then put a new board into place. In light of this, the BRP recommends that the FAF and the FASB take, or in some cases continue to take, certain actions that can be implemented in the short term or can be transitional actions to achieve needed near-term relief for private companies and help ensure a successful transition to the model and structure that the Panel recommends. The BRP believes that these actions, in whole or in part, do not change its recommendations for fundamental changes or the urgency needed to enact them.

Those recommendations are:

1. The FAF should fill at least one of the currently open board positions with individuals who have primarily private company background and experience.¹²
2. The FASB should continue to work closely with the PCFRC or another similar dedicated work stream. It should continue to have one or more board members present at each PCFRC meeting. PCFRC recommendations on Exposure Drafts and other matters should be discussed specifically at open FASB Board meetings.
3. In the short term and continuing as transitional actions until a new board is in place, the FASB should perform the following:
 - Continue to hold separate private company roundtables for major projects at locations around the country.
 - Incorporate private company concerns expressed at roundtables and in comment letters in the ongoing projects to evaluate whether there should be differences in recognition, measurement, presentation, disclosures, and/or effective dates. In view of publicly expressed concerns, if the board decides that there should be no differences, a clear explanation of their reasoning should be included in the basis for conclusions section of the final standards.
 - Consider a delay for private companies in the effective date of major new standards, especially those issued in connection with the FASB-IASB Memorandum of Understanding (MOU) projects, that is longer than the now-routine one-year delay.¹³

These processes described above will most likely continue once the new board is in place but will be led by and/or significantly involve the new board.

4. The BRP recommended that differences in GAAP for private companies be based on a framework (set of decision criteria). Using what it has learned from the two recent roundtables on private company issues with existing GAAP standards as key input, the FASB should begin to articulate “what differentiates private companies from public companies.” This articulation would be used to create the differential framework for private company accounting. The framework would be used to determine whether differences for private companies should be approved.

¹²The BRP acknowledges that on January 14, 2011, the FAF announced the appointments of two new FASB members, one of which has substantial experience as a private company CFO and the other of which has substantial experience as a user of financial statements, including financial statements of private companies.

¹³The delay would be with respect to the public company effective date. Thus, if, for example, the effective date for a particular MOU project is 2014 for public companies, this recommendation would contemplate an effective date of 2016 or later, rather than 2015, for private companies.

The FASB Board and staff could do much of this work, perhaps with the assistance of an appropriate, broad resource group, even before a decision by the Trustees on a desired model and board structure is finalized. The broad resource group should include significant user representation.

If and when a new board is established, it could then complete this work or, if already completed, could review it and either ratify it or revise it.

5. The FASB should look at the public comment process in its standard setting and consider taking steps to make it simpler to encourage responses by a broad base of stakeholders.

FAF and FASAC Structure

The BRP also believes that it is important that the FAF reassess the composition of its Board of Trustees to see that it has an appropriate number of members from the private company sector, including small and mid-sized private companies, to ensure its ability to reach out to and consider the needs of private companies in its oversight of the FASB and, if approved, a new private company standard-setting board.

In order for the FASB to consider private company needs in the standard-setting process, the FAF should reassess the composition of the FASB's primary advisory body, the Financial Accounting Standards Advisory Council (FASAC), to ensure that it has an appropriate number of members from the private company sector, including small and mid-sized private companies, to ensure its ability to consider the needs of the private company sector when providing strategic and other input to the FASB.

Marketplace Solution

In addition to its primary recommendations on private company accounting standards, BRP members generally believed that allowing the marketplace to effectively and efficiently function and allowing choices for private companies would prove to be a successful course for standard setting to follow. If GAAP with exceptions and modifications for private companies were developed, the choice of which version of GAAP a private company would apply—the set of standards under the new board's authority ("private company GAAP") or the set of standards under the FASB's authority ("FASB GAAP")—should be market driven, rather than set by the standard setters themselves.¹⁴ If the users of a private company's financial statements demanded adherence to FASB GAAP, that would be a cost-benefit decision that the company would have to make in consultation with the users of its financial information. Some regulated private companies (such as privately-held financial institutions) could be required, by statute or otherwise, to adhere to FASB GAAP in order to comply with specific industry requirements. Regardless of these situations, the standard setter would not be the decision maker; rather, the decision of which GAAP a private company (if not subject to regulatory requirements) should

¹⁴For example, both IFRS for SMEs and Canadian GAAP for Private Enterprises specifically preclude all financial institutions, including those that are privately held, from using those standards.

use would be in the hands of the company and its financial statement users. The BRP believes there should be a market-driven choice as to whether a private company would follow GAAP as set by the FASB or private company GAAP.

VI. ALTERNATIVE VIEWS

Dissenting View

One BRP member dissents from the BRP's recommendations for differential standards for private companies and a separate private company standard-setting board. This member's dissent may be found following Section VII.

Minority View

A small minority of BRP members, while generally agreeing with the other recommendations contained in this report, believe that the FAF should not create a new board but instead:

- Allow sufficient time to determine whether the recent changes in the FASB staffing and processes (see Appendix F) have improved the systemic issues of relevance, complexity, and the cost of certain standards
- Restructure the Board, and its processes, as necessary to help ensure that it produces accounting standards that meet the needs of users of private company financial statements in a manner that is cost-effective for both users and preparers
- Implement the actions described in Section V to achieve the best possible outcome for private companies.

These members believe that a decision to create a separate board is premature at this time because of the number of changes the FASB is currently implementing and the uncertainties about the future role of the FASB concerning public companies. These members feel that the FAF in its oversight role, including its post-implementation reviews, should hold the FASB fully accountable for standard-setting activities that achieve an appropriate cost-benefit balance for private companies, minimizing irrelevant information for users of private company GAAP financial statements and reducing the complexity of GAAP where appropriate for private companies, and likely for public companies as well. (Indeed, these members believe that the BRP's recommendation concerning a separate board may well have been different if the concerns of both public company stakeholders and private company stakeholders had been considered by the BRP as being under its purview.)

These BRP members also recommend that the FAF examine the FASB's composition and adjust as necessary to ensure that the Board includes members with sufficient private company experience and perspective to appropriately consider private companies in the standard-setting process. These BRP members recommend that the FAF explore the following restructured FASB Board scenarios as alternatives to a new board:

- As the FAF has already announced, increase the FASB board size to seven members from the current five and ensure that at least one member has primarily a private company background.¹⁵ Or, the FAF could further expand the FASB and increase the proportion of members with primarily private company backgrounds.
- Regardless of changes to the FASB Board, create an advisory task force structure (work stream) with the ability to effectively consider and determine exceptions and modifications in GAAP for private companies. In this scenario, the structure's decisions are subject to FASB Board ratification. This approach is akin to the way the FASB Board ratifies decisions of its Emerging Issues Task Force.

These BRP members believe that a single board, coupled with the enhancements noted in Section V of this report, provides the best opportunity for improving the standard-setting process for all companies. A single group of individuals that collectively has broader experience and perspective regarding private as well as public companies, along with the help of an advisory task force structure that can supplement the board composition and bring the needed focus and perspective for the private company constituency, will overcome the systemic issues in standard setting. These BRP members also feel that a single board lessens the risk of unintentionally diverging to a separate set of private company GAAP standards.

VII. BRP CONCLUDING COMMENTS

The BRP has spent a considerable amount of time developing recommendations that we believe will help address how accounting standards can best meet the needs of users of U.S. private company financial statements. We are pleased to be able to present our report to the FAF and hope that our conclusions and recommendations will be helpful to the FAF Trustees as they strategically address the standard-setting system for private companies.

We believe that significant improvements to the system are urgently needed, and we stand ready to assist in any way that we can to help ensure expeditious, beneficial change.

¹⁵The BRP acknowledges that on January 14, 2011, the FAF announced the appointments of two new FASB members, one of which has substantial experience as a private company CFO and the other of which has substantial experience as a user of financial statements, including financial statements of private companies.

DISSENTING VIEW

Teri Lombardi Yohn dissents from the recommendations of the Blue Ribbon Panel on Private Company Financial Reporting suggesting the establishment of differential standards for private companies and a separate private company standard-setting board. According to the FASB's Conceptual Framework, the objective of financial reporting is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders, and other creditors in making decisions about providing resources to the entity. In addition, financial reporting should provide information to help users assess the amount, timing, and uncertainty of future cash flows as a result of providing resources to the entity.

In the view of Ms. Yohn, there has been no compelling evidence presented to the Panel to suggest that the objectives of financial reporting are not being met for private companies. An argument presented to the Panel in support of differential standards is that users of private company financial statements are more likely to be lenders than equity holders and that U.S. GAAP focuses on information needs of equity investors. However, financial statements presented under U.S. GAAP are intended to provide decision-useful information for external users in general, and the Panel has not been presented with arguments or evidence that private company financial statements do not meet the needs of users. In fact, the push for differential standards has not been driven by users of private company financial statements, suggesting that the financial statements are providing decision-useful information.

There has also been no compelling evidence or framework presented to the Panel to suggest that the objectives of financial reporting differ between private companies and public companies. The Panel has merely been presented with a list of standards that accountants associated with private companies do not find desirable. The specific standards that have been highlighted are those related to fair value, uncertain tax positions, variable interest entities, and financial instruments. Public companies have similar concerns about the same standards. This suggests that perhaps these standards need to be reviewed to determine if they meet the objective of financial reporting. If the concerns over these standards are valid, then the standards should be improved for both private companies and public companies.

Proponents of differential standards for private companies suggest that some of the standards under U.S. GAAP are not relevant and/or are not cost beneficial for private companies and, therefore, that all private companies should be exempt from these standards. There is potentially a basis for differentiation of financial reporting for different classes of entities; however, the Panel has not been presented with evidence suggesting that there are sufficient similarities among private companies to warrant general exemptions. In addition, the Panel has not been presented with evidence to suggest that there are sufficient differences between private companies and public companies to warrant different standards for private companies. For example, there has been no analysis presented to the Panel suggesting that the differences for private versus public companies are any more significant than differences across other classes of companies, such as industry membership. The relevance of a standard should be judged on the basis of whether it meets the objectives of financial reporting. Without evidence that the financial reporting objectives differ between private companies and public companies, there is no basis to conclude that the relevance of standards differs across private and public companies.

There have been concerns presented to the Panel about the complexity of the standards under U.S. GAAP. However, the complexities in U.S. GAAP arise from an attempt to best capture the economics of the business and its transactions. By applying more simplified standards, the economics of the transaction are not likely to be captured in the same meaningful manner. If the economics could be captured more simply, then the standards for public and private companies should be modified to do so.

Proponents of differential standards for private companies focus on the costs and benefits of applying standards from the company's perspective. The proponents have considered only the cost of providing financial information and having the information audited. This is a narrow view of the costs and benefits associated with financial reporting. It is important to note that not providing relevant information to financial statement users can also be costly. In addition, establishing separate standards for private companies will add significant complexity and cost to other dimensions of financial reporting. For example, differential accounting standards will make it more costly for users to understand, standards setters to develop and maintain, educators to teach, and assurance providers to obtain proficiency in financial reporting.

Establishing differential standards for private companies will also reduce the comparability of financial statements. It is widely accepted that comparability of financial statements between entities, and over time for a given entity, enhances the decision usefulness of the information. The FASB's Conceptual Framework suggests that comparability is the principal reason for the development of accounting standards. Allowing for differential standards for private companies will reduce comparability across public and private companies. In addition, given that private companies would be allowed to follow either U.S. GAAP or private company standards, the comparability of financial reporting will be diminished even across private companies supplying audited financial statements.

Proponents of differential standards for private companies raise a concern over the number of qualified opinions that have been issued for private companies. However, given that there is no regulatory requirement to file audited financial statements for most private companies, these companies can choose to not prepare financial statements under U.S. GAAP if it is not beneficial. If a company chooses to apply U.S. GAAP, then the company should recognize that U.S. GAAP was established to best capture the economic position and profitability of a company. This is the "gold standard." There is no reason to modify the standards so that companies can get unqualified opinions. This is like writing an exam so that every student gets 100 percent. Just as formulating exams so that everyone would obtain a perfect score would make a mockery of exams, writing standards so that all companies get unqualified opinions would make a mockery of the standards. It is much better for a company to be held to the gold standard and have audit qualifications that explicitly state the standards that the company chose not to apply. This is more informative and transparent than having a differential set of standards with general exemptions. If private companies do significantly differ from public companies in terms of cost-benefit analyses of specific standards, then perhaps these concerns should be addressed through modifying the auditing standards and/or types of qualifications issued rather than through establishing a separate set of standards.

In summary, the Panel has not been presented with compelling evidence that the financial reporting objectives for private companies are significantly different from the objectives for

public companies. The Panel has also not been provided with guiding principles or compelling evidence to elicit how the financial reporting needs of users of private company financial statements differ from those of public company financial statements. The Panel has merely been presented with opinions as to what standards are preferred by accounting practitioners associated with private companies. Differential accounting standards for private companies will add significant complexity and cost to financial reporting. Given these costs, it is the responsibility of proponents of differential standards to articulate underlying principles and to provide compelling evidence to suggest that such a change is warranted.

For these reasons, Teri Yohn has concluded that, absent supporting evidence, there should be one set of U.S. GAAP standards and one standard-setting board. She thinks that changes could be made to the structure of the FASB and the supporting staff to better incorporate the views of private companies into the standard-setting process. Given the arguments and evidence presented to the Panel, Teri Yohn sees no basis to support the establishment of differential standards or a separate standard-setting board for private companies.

APPENDIX A

About the Blue-Ribbon Panel (BRP)—Mission, List of Members, Participating Observers, and Staff

I. Blue-Ribbon Panel Overview

As mentioned in the report’s Executive Summary, the American Institute of Certified Public Accountants (AICPA), the Financial Accounting Foundation (FAF, the parent organization of the Financial Accounting Standards Board (FASB)), and the National Association of State Boards of Accountancy (NASBA) established a “blue-ribbon” panel (the Panel or BRP) to address how accounting standards can best meet the needs of users of U.S. private company financial statements.

II. History

Three key factors led to the formation of the BRP:

- Summer 2009 FAF Listening Tour
- Fall 2009 AICPA Council meeting
- Fall 2009 Private Company Financial Reporting Committee (PCFRC) Letter to the FAF

Summer 2009 FAF Listening Tour

After John J. Brennan became Chairman of the FAF, he, other FAF Trustees, and FAF staff embarked upon a “listening tour” in various cities around the country in the summer of 2009 as part of the FAF’s strategic planning process. The team heard from all key stakeholder groups of the FASB. One of the primary lessons learned from this tour was the need for the FASB to improve its consideration of private companies’ views during the standard-setting process.

Fall 2009 AICPA Council Meeting

At its 2009 Fall Council meeting, the AICPA’s governing council discussed the current state of standard setting for private companies. More than 95% of Council members at that meeting supported differences in the GAAP applied by U.S. private companies, where appropriate, from GAAP applied by U.S. public companies (most of them strongly supporting such differences). Additionally, more than 90% said the idea of having a self-contained, standalone GAAP for U.S. private companies is worthy of major exploration.

November 2009 PCFRC Letter to the FAF

In November 2009, the PCFRC wrote a letter to the FAF recommending that it strategically consider the issue of U.S. private company accounting in the context of both the mission of the FASB and global developments, such as the creation of International Financial Reporting Standards (IFRS) for Small and Medium-sized Entities (SMEs) and Canadian GAAP for Private Enterprises. In its letter, the PCFRC indicated that its preferred approach was a separate, self-

contained set of standards for U.S. private companies tailored to the needs of statement users, though the FAF should explore other alternatives as well.

III. Composition and Outreach

The Panel is chaired by Rick Anderson, Chairman and CEO of Moss Adams, LLP, and FAF Trustee,¹⁶ and comprises 18 members. Panel Members are senior leaders who represent a cross-section of financial reporting constituencies, including lenders, investors, and owners, as well as preparers and auditors. All members have both extensive experience in their field and a keen and broad interest in financial reporting for private companies. In addition to the Panel members, the Panel has invited certain regulators and other key stakeholders to serve as participating observers for all of the Panel's work (see below for list of members, participating observers, and staff). The Panel also invited other guests to specific meetings for their expertise and perspective, and it solicited written submissions from the public on a series of questions on private company financial reporting.

¹⁶Mr. Anderson's term as an FAF Trustee ended as of December 31, 2010, due to term limits.

PANEL MEMBERS:

CHAIR:

Rick Anderson, Chairman and CEO, Moss Adams, LLP

MEMBERS:

Billy Atkinson, Board Chair, NASBA

Daryl Buck,¹⁷ Senior Vice President and CFO, Reasor's Holding Company, Inc.

Steve Feilmeier, Chief Financial Officer, Koch Industries

Hubert Glover, President and Co-founder, REDE, Inc.

David Hirschmann, President and CEO, Center for Capital Markets Competitiveness, U.S. Chamber of Commerce

William Knese, Vice President, Finance and Administration, Angus Industries

Kewsong Lee, Managing Director, Warburg Pincus

Paul Limbert, President and CEO, WesBanco, Inc.

Krista McMasters, CEO, Clifton Gunderson

Barry Melancon, President and CEO, AICPA

Jason Mendelson, Managing Director and Co-Founder, Foundry Group

Michael Menzies, President and CEO, Easton Bank and Trust Company

David Morgan, Co-Managing Partner, Lattimore, Black, Morgan, and Cain, PC.

Terri Polley,¹⁸ President and CEO, FAF

Dev Strischek, Senior Vice President and Senior Credit Policy Officer, Corporate Risk Management, SunTrust Banks, Inc.

¹⁷The BRP acknowledges that on January 14, 2011, the FAF announced the appointment of Daryl Buck to the FASB for a term beginning February 28, 2011. In light of this announcement, Mr. Buck resigned as a member of the Blue-Ribbon Panel on January 17, 2011, and did not participate in the final vote.

¹⁸Non-voting member.

PANEL MEMBERS: (continued)

Mark Vonnahme, Professor, University of Illinois; former Executive Vice President, Surety, Arch Insurance Group

Teri Yohn, Associate Professor, Indiana University

PARTICIPATING OBSERVERS:

Karen Kelbly, U.S. Federal Financial Institution Regulatory Agencies Group

Dan Daveline, National Association of Insurance Commissioners

Dillon Taylor, U.S. Small Business Administration

Judith O'Dell, Chair, FASB Private Company Financial Reporting Committee

Mark Ellis, Member and Agenda Subcommittee chair, FASB Small Business Advisory Committee

Russ Golden, Board member, FASB; former Technical Director, FASB

STAFF:

Jeffrey Mechanick, FAF/ FASB

Meredith Vogel, Grant Thornton LLP

Robert Durak, AICPA

Paul Glotzer, FAF/ FASB

Daniel Noll, AICPA

APPENDIX B

BRP Process—Agendas, Outreach, and Invited Guests

To accomplish its mission, the Panel held five in-person meetings, during which it considered:

- Previous studies and other reports on standard setting for U.S. private companies (see Appendix D)
- The current standard-setting system from the perspective of the various members, participating observers, invited guests, and the public (through a summary of the written submissions; see Appendix G)
- Efforts of global and other national standard setters concerning private companies
- Various alternatives to the current system, in terms of processes (models) and structures, including short- and longer-term actions that may be necessary for putting into place any desired alternatives (see Appendix H).

As part of its process, the Panel invited other guests to its meetings for their expertise and perspective on topics relevant to the Panel’s work and conducted an outreach effort to private company stakeholders.

I. Meetings Agendas and Minutes

[Meeting 1 – April 12, 2010 \(New York, NY\)](#)

The agenda for the Panel’s first meeting included a general overview session, including a history of the debate on private company standards within the U.S. financial reporting system and a brief overview of actions taking place in other countries on private company financial reporting. Panel members reviewed and discussed the current U.S. standard-setting process (see Appendix E) and previous studies and reports, especially the 2005 Private Company Financial Reporting Task Force Report (“Castellano Report”) (see Appendix D).

To better understand the views of and issues facing private company financial statement users, Panel members and participating observers representing a user perspective delivered prepared remarks to the Panel. The Panel discussed the following questions:

- Who are the actual users of private company financial statements?
- What is the key, decision-useful information that the various users need from GAAP financial statements? Is there information users don’t need or can’t get?
- Are current U.S. GAAP financial statements meeting those needs? Why or why not?
- Do users routinely “adjust” the GAAP financial statements to meet their needs?
- Are users concerned about the cost-benefit issues of preparing GAAP financial statements?

Meeting 2 – May 14, 2010 (Norwalk, CT)

The Panel continued its discussion about private company financial statement user needs and continued to hear testimony from those users, including a corporate director and a credit analyst. Panel members then heard the viewpoints of private company financial statement preparers and practitioners. Panel member preparers and practitioners delivered prepared remarks, and Panel members heard testimony from a “Big Four” practitioner. The Panel considered whether US GAAP is meeting private company user needs in a cost-effective manner for both users and preparers.

The Panel then looked at alternative private company financial reporting standard-setting processes in other countries in some detail. After receiving an overview of standard setting in other countries and regions, the Panel listened to a presentation about Canadian GAAP for Private Enterprises, a proposed standard-setting system for private companies in the United Kingdom, and a presentation about IFRS for Small and Medium-sized Entities. Afterwards, Panel members considered the following questions:

- How does standard setting for private companies in the U.S. compare to standard setting in other countries, both those that have adopted IFRS for Small and Medium-sized Entities and those that have not?
- To the extent that current U.S. GAAP is not meeting user needs in a cost-effective manner, what can the Panel learn from the alternatives seen in other countries?

Meeting 3 – July 19, 2010 (Chicago, IL)

After some additional discussion about the nature of the problems in the standard-setting system with respect to private companies, the Panel considered alternative models and structures for private company standard setting (see Appendix H). Panel members expressed their views on which alternative(s) was preferable and why, on whether there were any new or different alternatives not identified by staff, and on what structural changes, if any, would be needed to achieve the preferred model(s) and why.

The Panel also held a discussion about overarching issues surrounding the models and considered whether there should be scope limitations regarding the Panel’s recommendations, specifically:

- Should private companies with some form of public accountability or over a certain size be excluded?
- Alternatively, should this be left up to the U.S. marketplace, that is, to users and possibly regulators?

Meeting 4 – October 8, 2010 (New York, NY)

The fourth meeting began with Panel members learning about recent changes at the FASB (see Appendix F). After that, the Panel reviewed and discussed a summary of written submissions received from the public in response to the Panel’s outreach (see Appendix G).

The Panel then continued its discussion of alternative models and structures, while considering the following questions:

- Generally, which model is preferable in the long run and why?
- Given the amount of time required to achieve that model, are there other models (or aspects of other models) that should be considered as intermediate steps and why?
- What short-term and/or long-term structural changes are necessary to achieve the preferred model (or combination or sequence of models) and why?

After considering those questions, the Panel worked on reaching a consensus about which model and structure to recommend to the FAF.

Meeting 5 – December 10, 2010 (Norwalk, CT)

At its last meeting, the Panel worked on finalizing the details of its recommendations to the FAF, including a discussion about the new private company standards board's mission, role, structure, composition, protocols, budget, and funding.

The Panel also discussed:

- What other short-term and/or long-term actions may need to be taken by the FAF, FASB, or both?
- Are there any other recommendations that should be discussed by the Panel?

For further information, refer to the [Panel Meeting Minutes](#) webpage on the FAF's website.

II. Guests Invited to Panel Meetings

Meeting 1

- Paul Beswick (Deputy Chief Accountant for Professional Practice in U.S. Securities and Exchange Commission Office of the Chief Accountant)
- Jim Castellano (RubinBrown)

Meeting 2

- Keith Alm (National Association of Corporate Directors)
- Greg Edwards (Accounting Standards Board, Canada)
- Tom Jones (former Vice Chairman, International Accounting Standards Board)
- Joyce Joseph (Standard and Poor's)
- Ian Mackintosh (Chairman, UK Accounting Standards Board)
- Tricia O'Malley (Chairman, Accounting Standards Board, Canada)
- Joel Osness (Deloitte & Touche LLP)
- William Schramm (PricewaterhouseCoopers LLP)

Meeting 3

- Paul Beswick (Deputy Chief Accountant for Professional Practice in U.S. Securities and Exchange Commission Office of the Chief Accountant)
- John Perrell (Trustee, FAF)

Meeting 4

- Douglas Donahue (Trustee, FAF)
- John Perrell (Trustee, FAF)
- Leslie Seidman (Chairman, FASB)

Meeting 5

- Jeff Diermeier (Trustee, FAF)
- John Perrell (Trustee, FAF)
- Leslie Seidman (Chairman, FASB)

APPENDIX C

Recommended New Board Structure and Operating Protocol Chart

Function	Recommendation	Alternatives Considered	BRP Commentary
New board mission	The mission of the new board is to establish exceptions and modifications to GAAP for private companies, while ensuring that such exceptions and modifications provide decision-useful information to lenders and other users of private company financial reports. That mission is accomplished through a comprehensive and independent process that encourages broad participation, objectively considers all private company stakeholder views, and is subject to oversight by the Financial Accounting Foundation’s Board of Trustees.		Wording is consistent with FASB’s mission, but tailored to the specifics of this board.
New board model and how it works with the FASB	<p>New board has authority to modify existing and future GAAP for private companies, where appropriate.</p> <p>FASB board considers input from all companies (including private companies) during the standard-setting process.</p> <ol style="list-style-type: none"> 1. The goal is the FASB should try to produce the best possible standard for all entities (public companies, private companies, not-for-profit entities). 2. The new board has the responsibility for outreach to private company stakeholders, and it provides input to the FASB Board along the way so that the FASB can produce the best possible standards for all companies (both public and private companies). 		To some degree the new board and FASB will be best positioned to decide how to operationalize the promulgation of modifications and exceptions, depending on the facts and circumstances of a standard-setting topic.

Function	Recommendation	Alternatives Considered	BRP Commentary
	<ol style="list-style-type: none"> <li data-bbox="477 279 922 636">3. Nothing precludes the FASB on a current agenda project from receiving input directly from private company stakeholders, but the specific responsibility for seeking such input resides with the new board, which then shares the results of such outreach with the FASB. <li data-bbox="477 646 922 856">4. The new board reviews the product of the FASB and effectively endorses it or proposes modifications/ exceptions through its own due process. <li data-bbox="477 867 922 1161">5. The new board takes formal due process actions when it believes modifications/ exceptions are warranted beyond what the FASB has promulgated; otherwise, FASB output is accepted through non-action. <li data-bbox="477 1171 922 1465">6. The new board, not the FASB, ultimately authorizes modifications/exceptions in GAAP for private companies, but such differences may be promulgated within a FASB standard (with the support of the new board). <li data-bbox="477 1476 922 1644">7. The new board adheres to a differential framework to help ensure that there is no undue divergence in GAAP for public and private companies. 		

Function	Recommendation	Alternatives Considered	BRP Commentary
New board overall process	The new board works with the FASB throughout the standard-setting process; the new board conducts robust outreach to private company stakeholders when the need arises; it issues Exposure Drafts (EDs) when proposing modifications/exceptions. The boards can issue joint EDs on fast moving topics, thus allowing the FASB and the new board to propose modifications/exceptions within a joint ED; the FASB or the new board (which one depends on facts and circumstances) issues final standards for such differences that are then embedded in the Codification.	The new board issues a separate ED and final standard on everything the FASB (including EITF) does.	The BRP believes the two boards and staff should work together to ensure that GAAP remains a single “language” wherever possible, and that the FASB still should attempt to consider input from private company stakeholders with a goal of developing the best possible standard for all companies.
New board composition/ structure	Full-time chair, full- or part-time other members, Possibly 5 to 7 total members, 1–2 users 1–2 practitioners 1–2 preparers Possibly 1 academic		The FAF should consider the pros and cons of a full-time versus a part-time board. A full-time board would allow for greater independence while a part-time board would require less funding and could help the board members stay better connected with private company constituencies and private company financial reporting issues.
Staff composition	Staff should have primarily private company sector background. Some shared staffing with FASB desirable.		Staffing composition depends on the board’s structure and workload.

Function	Recommendation	Alternatives Considered	BRP Commentary
Board observers	Full-time new board chair or other member of new board attends all FASB board meetings as an official observer; the FASB designates one board member as an official observer to all new board meetings. Official observers have the right of the floor but do not vote.	Official observers have the right to vote (meaning they serve in effect as a board member).	Cross voting is impractical—for example, an observer might vote for something as part of the FASB Board and then would be hard-pressed to change his/her vote as a new board observer.
Advisory groups	The new board forms a primary advisory group—the PCFRC could possibly become such a body.		
New board governance	The FAF oversees the new board as it does the FASB/GASB; there is a 3–5 year sunset provision. The FAF increases the number of Trustees with private company stakeholder backgrounds; the FAF’s post-implementation assessment on FASB/GASB standards is also applicable to new board.		
Approximate budget	\$4–6 million; that could vary upward or downward subject to operating and structural specifics.		
Funding sources	A portion of FAF publications sales and mandatory contributory model from stakeholders (subject to further analysis, including legal).	State board licensing fee allocation.	An endowment approach might be an appropriate mandatory contributory model.

APPENDIX D

List of Previous Studies and Reports Considered by the BRP

The following is a list of previous studies conducted and reports issued by the FASB, various AICPA committees, and others concerning private company standard setting in the U.S. The Panel reviewed these as background information and discussed some of them during the course of its meetings.

1. *Report of the Study on Establishment of Accounting Principles*, AICPA, March 1972 (“Wheat Report”)
2. *Report of the Committee on Generally Accepted Accounting Principles for Smaller and/or Closely Held Businesses*, Accounting Standards Division of AICPA, Discussion Paper, August 1976
3. *Report of the Special Committee on Small and Medium-Sized Firms*, AICPA, 1980 (“Derieux Committee”)
4. *Tentative Conclusion and Recommendations of the Special Committee on Accounting Standards Overload*, AICPA, December 23, 1981
5. *Report of the Special Committee on Accounting Standards Overload*, AICPA, February 1983
6. a. Invitation to Comment, *Financial Reporting by Private and Small Public Companies*, FASB, November 1981
b. Special Report, *Financial Reporting by Privately Owned Companies: Summary of Responses to FASB Invitation to Comment*, FASB, 1983
7. Research Report, *Financial Reporting by Private Companies: Analysis and Diagnosis*, FASB, August 1983
8. *Standards Overload: Problems and Solutions*, AICPA, June 1995
9. *Report of the Private Companies Practice Section Special Task Force on Standards Overload*, August 1, 1996
10. *What Do Users of Private Company Financial Statements Want?*, Financial Executives Research Foundation, 1996
11. *Private Company Financial Reporting Task Force Report*, AICPA, February 28, 2005, and supplementary survey results:
 - a. Random Research Survey Results
 - b. Broad Outreach Survey Results
 - c. Comparison of Certain Random and Broad Outreach Survey Results
12. Invitation to Comment, *Enhancing the Financial Accounting and Reporting Standard-Setting Process for Private Companies*, FASB, June 8, 2006

APPENDIX E

Overview of the FAF and the FASB

The Blue-Ribbon Panel on Standard Setting for Private Companies (the Panel) was formed to develop a recommendation to the [Financial Accounting Foundation \(FAF\)](#) addressing accounting standards for private companies and the standard-setting process used to develop those standards.

Organized in 1972, the FAF is the independent, private-sector organization with responsibility for:

- Establishing and improving financial accounting and reporting standards
- Educating stakeholders about those standards
- The oversight, administration, and finances of its standard-setting Boards, the [Financial Accounting Standards Board \(FASB\)](#) and the [Governmental Accounting Standards Board \(GASB\)](#), and their advisory councils
- Selecting the members of the standard-setting Boards and advisory councils
- Protecting the independence and integrity of the standard-setting process.

Although the FAF has responsibility for establishing and improving financial accounting and reporting standards, it does not set those standards. That responsibility falls on the two Boards it oversees, the FASB and GASB. The FAF's role is to ensure that the Boards are independent and act with objectivity and integrity through an open due process which encourages active and collaborative involvement from all interested parties. It accomplishes that role through the oversight, administration, and financing of the Boards and their advisory councils, the [Financial Accounting Standards Advisory Council \(FASAC\)](#) and the [Governmental Accounting Standards Advisory Council \(GASAC\)](#). The FAF recently augmented its oversight procedures by establishing a formal post-implementation review process for the standards issued by the two Boards.

The Financial Accounting Standards Board (FASB), established in 1973, has been the designated organization in the private sector for establishing standards of financial accounting that govern the preparation of financial reports by nongovernmental entities. The FASB's mission is to establish and improve standards of financial accounting and reporting that foster financial reporting by nongovernmental entities that provides decision-useful information to investors and other users of financial reports.

Accounting standards issued by the FASB have been recognized by the U.S. Securities and Exchange Commission (SEC) as generally accepted for federal securities law purposes. State Boards of Accountancy and the AICPA have also recognized those standards as GAAP for financial statements of nonpublic entities.

For more information, the FAF website provides an [overview](#) of the FAF, with additional links to information about its officers and Trustees and contact information. For additional information about the FASB, the FASB website provides an [overview](#) of the FASB, with links to information about the [Members of the FASB](#) and its [Rules of Procedure](#).

APPENDIX F

Recent Changes at the FASB

Since mid-2009, the FASB has made, and has continued to make, changes to bring greater focus on and otherwise improve its standard-setting activities with regard to the private company sector. FASB Board Chairman Leslie Seidman reported on these activities during the October 8, 2010, and December 10, 2010 BRP meetings.

Some of the key changes have involved augmenting the staff dedicated to private companies. In June 2009, the FASB appointed an assistant director who is responsible for strategic and technical oversight of private entity issues, including those of both private business entities and not-for-profit organizations, in addition to the project manager who was already dedicated to private company issues. In the last half of 2010, the FASB reassigned three other staff members to the private entities team to help address private entity issues throughout the FASB's projects, especially its Memorandum of Understanding projects with the IASB.

In August, 2010, the FAF announced that the FASB Board would increase in size from five members to seven members, with a private company background being one of the focal areas in recruiting for the new members. Among other benefits, the additional members will enable the Board to do more outreach through meetings and conferences attended by representatives of the private entity constituencies.

Beginning in 2010, a Board member started attending all meetings of the Private Company Financial Reporting Committee (PCFRC) to hear firsthand about private company issues arising from proposed standards. The interaction between the PCFRC and the Board benefits both groups, and thus the standard-setting process. The Board gets a better understanding of the issues and hears potential solutions. The PCFRC hears from a Board member why the Board has made the decisions it has made.

Outreach activities have been expanded in other ways to obtain more information specifically from the private company perspective. For the major projects, the Board and staff meet with private companies in field visits. To illustrate, the Financial Statement Presentation project team with help from the Technical Issues Committee (TIC) of the AICPA Private Companies Practice Section obtained financial statements from approximately 20 private companies, representing various industries, that recast the statements from the current presentation model to the proposed model. The recast statements were used in a study to see whether those statements resulted in better information for making lending decisions. A panel of 20 users of private company financials was assembled to provide feedback on those recast financials. The Board and staff are also now conducting public roundtables for various projects to hear specifically from the private entity constituencies about their issues and concerns on proposed standards.

The FASB held roundtables in October and November 2010 to hear about private company concerns with existing GAAP. Two items on the agenda were FIN 48, *Accounting for Uncertainty in Income Taxes*, and FIN 46R, *Consolidation of Variable Interest Entities*. The format of the roundtables allowed for users, practitioners, and preparers to discuss issues with the Board and help give insight as to what information is useful, and how it can be provided cost-

effectively. Another issue raised was the use of fair value by private companies, especially with regard to impairment testing. At the December 10th Panel meeting, Ms. Seidman stated that the FASB had added a near-term project to its agenda to look at this issue.

Other activities designed to better serve private entities include the use of plain English in webcasts, podcasts, and Twitter feeds to help educate them about the FASB's projects and to solicit more participation by them in the standard-setting process.

Ms. Seidman stressed that these actions show that the Board is committed to understanding private company issues and incorporating a careful consideration of them in the standard-setting process.

APPENDIX G

List of Respondents to Questions Posed by the BRP and Summary of Written Submissions

WRITTEN SUBMISSIONS FROM THE PUBLIC

List of Interested Parties Who Responded to Questions Posed by the Blue-Ribbon Panel (in order received)

Letter	Affiliation or Individual¹⁹
1	Thomas Malkoch
2	Jodi Gill
3	Russell Abernathy
4	Carl Bagge
5	Jeremy Veilleux
6	Lance Mann
7	Laura Lewis
8	Lauren Barnet
9	Frankel And Topche, PC
10	Joan Waggoner
11	Anonymous
12	Bruce Benator
13	O'Sullivan Creel, LLP
14	Jay Tolsma
15	David Wagner
16	Todd Lisle
17	Morris, Kalish + Walgren, P.C.
18	Howard Bornstein
19	Mike Sedam
20	Gross, Mendelsohn & Associates, P.A.
21	Michael Nesland
22	Ken Posner
23	Peter Kwong
24	Philip Stoler
25	Ernest Lapp
26	Frank Minter
27	Flexco
28	Nancy Mcclarey

¹⁹Some of the respondent letters were grouped together by affiliation.

Letter	Affiliation or Individual
29	Shaun Bawden
30	Scott Robinson
31	Peter Philbrick
32	Eric Smith
33	Scott Womble
34	Brenda Smith
35	Carl Chatto
36	Michael Atkins
37	Medina Company, PSC
38	Theodore Medrek
39	Parentebeard, LLC
40	David Johnson
41	Carol Uhl
42	Quick & Mcfarlin, P.C.
43	Garry Hutchison
44	Larry Sample
45	Art Thielen
46	Robert Foley
47	Steve Freimuth
48	Doug Knights
49	Leatham & Associates, CPAs
50	Curtis Root
51	Doug Hawkes
52	Withumsmith+Brown P.C.
53	Alan King
54	Doug Chaffins
55	Hoots, Baker & Wiley, PC
56	Tommy Thomson
57	David Frizzell
58	Charles Postal
59	James Lagana
60	Stu Harden
61	Steve Rabin
62	Caler, Donten, Levine, Porter & Veil, PA
63	Bart Tiffany
64	Vickie Martin
65	Gish Seiden, LLP
66	Candido Fernandez

Letter	Affiliation or Individual
67	Michael Moore
68	Sherman Rosenfield
69	Hogan - Hansen, PC
70	David Hurley
71	Doug Donaghue
72	Mahesh Chithkala
73	Cherry, Bekaert & Holland, LLP
74	David Strottmann
75	Susan Ryan
76	Culver Lamb
77	National Rural Electric Cooperative Association
78	Steve Morris
79	National Cooperative Business Association
80	Kennedy And Coe, LLC
81	Arthur Hendricks
82	Institute Of Chartered Accountants In England And Wales
83	Yeo & Yeo CPAS and Business Consultants
84	Dee Brown, Inc.
85	Stan Sterk
86	Packer Thomas
87	Mike Beach
88	Don Lueger
89	O'Brien Energy Company
90	Deseret Power
91	Kreston International
92	Vickie Beer
93	Ernst & Young LLP
94	The Madray Group
95	John Litchfield
96	Beach Fleischman
97	Jerry Mcmillon
98	Steakley & Gilbert, P.C.
99	Prather Kalman, P.C.
100	Geoff Flynn
101	Jerry Woods
102	Tom Hoey
103	Heidi Lee
104	Patrick Murry

Letter	Affiliation or Individual
105	David Baugh
106	David Kasuba
107	Bart Adams
108	James Branch
109	Karen Keller
110	Pricewaterhousecoopers
111	Pennsylvania Institute of Certified Public Accountants
112	Financial Executives International, Committee on Private Company Standards
113	Barfield Murphy Shank & Smith, P.C.
114	Munninghoff, Lange and Company
115	Clifton Gunderson, LLP
116	Deloitte & Touche, LLP
117	Anders Minkler & Diehl, LLP
119	Ohio Society of Certified Public Accountants
120	John Mcdaniel
121	Texas Society of Certified Public Accountants
122	Susie Repko
123	Pershing Yoakley & Associates, P.C.
124	Rea & Associates, Inc.
125	Ima/Sbc
126	Marc Porter
127	Plante & Moran PLLC
128	Emilio Colapietro
129	Maryland Association of Certified Public Accountants
130	Mark Blackburn
131	James Pistillo
132	Ted Lodden
133	Illinois CPA Society
134	Battelle & Battelle, LLP
135	California Society of Certified Public Accountants
136	Hines Interests L.P., Southwest Region
137	Weisermazars, LLP
138	Harry Drew
139	Sensiba San Filippo, LLP
140	Fort Pitt Group, LP
141	Barnes Wendling CPAs
142	Crowe Horwath, LLP
143	Clark Nuber P.S.

Letter	Affiliation or Individual
144	Grant Thornton, LLP
145	Piercy Bowler Taylor & Kern, CPAs
146	McGladrey & Pullen, LLP
147	Managed Health Care Associates, Inc.
148	KPMG, LLP
149	Great American Insurance Company, Contract Surety Division
150	CPAmerica
151	Federal Financial Institution Regulatory Agencies

RESPONDENT PROFILE

1. As of October 1, 2010, the Panel received written submissions from 148²⁰ respondents. Three additional response letters (#149–151) were received after October 1, 2010, and were not included in the summary below but were discussed at the October 8, 2010 BRP meeting. Certain key aspects of letter #151 have been included in the body of the report. The entire respondent population has been identified below:

Respondent Type	Number of Respondents	Percentage
CPA firm with fewer than 5 partners (including sole practitioners)	36	24%
CPA firm with 6 to 20 partners	26	17%
CPA firm with 21 to 100 partners	13	9%
CPA firm with 101 to 500 partners	5	3%
CPA firm with over 500 partners	6	4%
CPA firm, size not specified	11	7%
Lender	2	1%
Owner	2	1%
Preparer	15	10%
State CPA society	6	4%
Trade organization	4	3%
Regulator	1	1%
Other (anonymous or not specified)	24	16%
TOTAL	151	100%

²⁰Some of the respondent letters were grouped together by affiliation.

SUMMARY OF RESPONSES

2. The opinions of respondents varied considerably. Given the quantity of the comment letters, the following sections are meant to highlight common themes they presented.

QUESTIONS FOR SUBMISSIONS

All respondents:

Question 1: Please complete the attached form to help compile information on the respondents and send as a separate attachment.

3. See above respondent profile.

Question 2: Users (e.g., lender, surety, investor, owner) only:

a) Briefly describe how you use U.S. GAAP financial statements in your decision making concerning private companies.

4. One trade organization indicated that users use GAAP financial statements as one of their tools to monitor a company's performance and to ensure that they have a complete picture of the company. A member of a different trade organization said they use financial statements to look for "red flags" but not much else. This member felt that financial statements provide some comfort but also mentioned that users didn't feel that GAAP financial statements are very useful.
5. Another trade organization felt that GAAP financial statements are not a desired tool for operating an enterprise.
6. Lenders stated that they use financial statements to analyze a customer's financial position to make appropriate lending decisions. One lender stated that the majority of its customers prepare financial statements on a cash or tax basis.
7. One owner stated that they only use GAAP financial statements once a year to share the results with their employee owners and with their bankers. This owner further discussed certain GAAP accounting requirements that would terribly misstate information if the owners used the statements to manage the business.

b) Tell us about any issues or concerns that you may have with respect to the relevance of the information contained in those statements. Please be as specific as possible in your answer.

8. Many of the trade organizations commented that there is an overload of financial information in GAAP financial statements that is not relevant. One trade organization felt that if GAAP financial statements were simplified, it would be more useful to small and private companies from an operational perspective.
9. One lender felt that if all financial statements were prepared in the same fashion, it would help make decision making more uniform. However, in reality, a "one size fits all" approach in relation to GAAP financial statements does not work. This

lender stated that fair value accounting is not relevant to an investor and owner and that it frequently increases accounting costs and confusion.

Question 3a: Tell us about any issues or concerns you have with current U.S. GAAP accounting standards as those standards apply to private company financial statements.

Lack of relevance to users

10. CPA practitioners with fewer than 5 partners shared several concerns about the relevance of U.S. GAAP to private companies. These respondents generally shared a view that there is a disconnect between private companies and the standard-setting process that has led to reporting requirements that do not seem to be useful or relevant to the users of private company financial statements.
11. These small CPA practitioners also stated that the users, generally banks and bonding companies, are interested in financial information that can help them determine the amount, timing, and uncertainty of cash flows. Many of the most costly standards for private companies to implement contain complex disclosures that focus on information that their users do not understand and which does not provide value to the users. One respondent suggested that their bankers will often ignore fair value disclosures because of this reason. This point is further demonstrated by the fact that many users have been accepting of financial statements that are prepared on an other comprehensive basis of accounting (“OCBOA”), usually the tax basis.
12. CPA practitioners with 6 to 20 partners shared some of the views above. Some of these respondents noted that accounting standards are primarily designed to meet the needs of equity analysts. There are certain disclosure requirements that do not provide any incremental benefit to the users of private company financial statements. For example, these users will not be concerned about how a stock price increases in value based on how a company performs. These respondents maintained that different users have distinct needs, and that the current accounting standards are not fulfilling the needs of users of private company financial statements.
13. Most CPA practitioners with 21–500 partners also agreed that the public company focus of standard-setting activities leads to complex accounting and that ultimately provides little benefit to many users of the financial statements.
14. Certain CPA practitioners with over 500 partners shared the general concern that some standards are not relevant to certain users. However, these respondents arrived at some different conclusions. One such respondent noted that, broadly speaking, accounting should faithfully represent the economics of an underlying transaction. As a result, recognition and measurement should be based on the transaction itself and applied consistently regardless of the nature of the reporting entity. Moreover, there is a benefit to using consistent standards as a private company grows and becomes more similar to its public counterparts. This respondent noted that both private and public companies have questioned the relevance of certain standards, at times the same standards, to the decision making of their users and further concluded that the improvements and changes should relate to all companies.
15. CPA practitioners with over 500 partners also felt that the issue of relevance is not confined to private company financial reporting. Echoing the sentiments of the other

- CPA practitioners' responses, they noted that public and private company financial statement user needs vary by user. However, users are already currently equipped to deal with this, and they have the ability to adjust financial statements prepared under GAAP to tailor them and eliminate the effects of certain standards that they do not find relevant.
16. Responses from lenders expressed a similar view that information they look for depends on the specific entity, and a "one size fits all" approach would not be able to fulfill their needs.
 17. A preparer respondent stated that "we do not use GAAP financial statements for any business decision making in our capacity as asset manager or investor" and that GAAP financial statements provided little value to their particular user group. Another stated that:

"In theory, if all financial statements were prepared the same, it would simplify the analysis of the information and make decision-making more uniform. However, in application, this is not practical. One size does not fit all. There is a cost/benefit perspective that needs to be applied. And relevance becomes the overriding issue."
 18. Trade organizations shared similar sentiments to the CPA practitioners above. One respondent specifically pointed out that as fair value becomes more embedded into the balance sheet, the assets and liabilities that are presented do not translate into future cash flows. As a result, users find it difficult to make sense of that information.
 19. Owners expressed a lack of interest in the GAAP financial statements. One respondent stated that the GAAP financial statements were used only once a year to share results with their owners. Owners and lenders have a historical cost perspective, and the information they are interested in is not being captured by the financial statements.

Complexity and pace of standard setting

20. CPA practitioners with fewer than 5 partners generally agreed that there were challenges related to not only the complexity of standards but to the recent pace of standard setting. Many respondents found that complexity not only led to difficulty for their clients in preparing the financial statements but also to a lack of understandability by internal and external users. Some respondents felt that the disclosures required by GAAP are incomprehensible to both the average reader and even some sophisticated users. At the same time, the increased pace of standard setting recently has only served to intensify this issue. Respondents explained the difficulty of keeping abreast of new Exposure Drafts issued by the FASB. These respondents have found it challenging to find the means to comment on Exposure Drafts and to participate in the stages of due process.
21. CPA practitioners with fewer than 5 partners also believed that the complexity of the standards are exposing firms to additional liability and risk because they do not have the in-house capabilities and time to stay abreast of the changing standards.

22. CPA practitioners with 6 to 20 partners echoed the sentiments about the complexity of standards. One practitioner felt that the new and complex accounting standards have placed an unnecessary burden on small businesses and CPAs.
23. A CPA practitioner with 21 to 100 partners also noted that the increased complexity of accounting standards has been causing clients to rely more heavily on CPA firms, potentially causing independence issues.
24. CPA practitioners with over 500 partners shared many of the same concerns about complexity. One practitioner felt that the increase in complexity was partly due to the increasing complexity of business transactions and partly due to certain disclosure requirements that have become too burdensome.
25. Several CPA practitioners, varying in firm size, and trade organizations were concerned about the increasing frequency with which proposed standards are being issued. One practitioner stated that it appeared the window of time during which FASB accepts comment letters had decreased. In addition, the pace of change makes it more difficult to keep up with and evaluate the applicability of new proposals. Other practitioners and preparers also claim that the timing of certain standards was rushed. As such, there has been an increase in revised standards and numerous staff positions (now ASUs) to help deal with complexities that they felt were not addressed prior to the initial release of the standards.
26. Chief financial officers and a respondent from a state CPA society felt similarly that accounting standards had become too complex for the average accounting department at a private company and frequently were beyond the expertise of their auditors. One CFO stated that:

“Those of us out in the economy doing day in and day out financial reporting find it almost impossible to even keep up with the changes in GAAP and what current GAAP applies to our companies’ (sic) situations and financial transactions. Most people, no matter how well educated, cannot read much less understand a GAAP financial report ... they are for use by the “financial elite” who probably do not understand them either.”
27. A preparer responded that the biggest challenge was not the complexity of the standards themselves but rather having to provide the necessary education for private sector accountants.

Costs exceed benefits

28. CPA practitioners with fewer than 5 partners generally agreed that the cost of preparing GAAP financial statements has increased compared to the perceived benefits that certain new standards have brought to financial reporting. One practitioner felt that “there seems to be no consideration of the cost to implement a standard, whether in terms of internal resources, external costs or even the ability of the CPA to get paid for the additional work necessary to conform a client to new standards.” Practitioners in the same group felt that the FASB is so concerned with public companies that they do not consider the cost to implement certain standards with respect to private companies. They believed the cost to pay for external valuation analysis such as goodwill impairment, acquisition accounting, and stock

- compensation is a greater financial strain for private companies than for public companies.
29. CPA practitioners with 6 to 20 partners generally agreed that the benefits do not exceed the costs because private company users have the ability to confer directly with management. This group also believed that if private companies were subject to a limited or simplified set of standards, companies would benefit because they would be more apt to have a financial statement audit. These practitioners felt that many of their clients rely on the CPA firm to draft their financial statements, so the compliance costs and CPA firm's liability goes up. Generally, this group felt that the new standards are placing an undue financial burden on many private companies while there is no perceived benefit for private company users.
 30. CPA practitioners with 100 to 500 partners also generally felt that the cost of GAAP financial statements often exceeds the benefits. One practitioner felt that the costs that private companies incur to obtain technical knowledge to comply with GAAP and to be able to prepare GAAP financial statements outweigh the benefits.
 31. CPA practitioners with 500 or more partners felt that the FASB should develop concepts to help the standard setting with cost-benefit analysis. One practitioner in this group stated that "private companies face different cost/benefit considerations that make it difficult to justify application of certain aspects of U.S. GAAP." Another practitioner suggested that the cost-benefit considerations could differ between public and private companies, which could justify disclosure differences for private companies.
 32. Another CPA practitioner with 500 or more partners stated that "because the needs of private company users may be different from those of public company users, we encourage the FASB to increase its outreach to private company preparers, users, and auditors to better ascertain the costs and benefits of applying new accounting standards. The feedback received will help the FASB better evaluate the situations in which divergence in the guidance for public and private companies is appropriate. Disclosure, transition, and effective dates are examples of areas in which such divergences may be warranted."
 33. Some trade organizations felt a cost-benefit analysis based on some clearly defined parameters to help guide deliberations on new standards may help with cost-benefit considerations. Another trade organization felt that companies without audited financial statements pay a premium to obtain capital.
 34. A lender response also pointed out a concern relating to unintended consequences of new GAAP as it relates to regulatory requirements. The lender noted that, often, changes in GAAP will lead to changes in the regulatory requirements to which a private company must adhere. However, in many of these cases, the regulatory requirements will not consider materiality thresholds, and private companies will become subject to extensive and sometimes onerous regulatory reporting.
 35. One chief financial officer felt that accounting standards such as fair value are not useful to the users and compliance costs are going up to comply with such standards.

Increasing Qualified Opinions and use of OCBOA

36. Some CPA practitioners expressed concerns about the increasing number of qualified opinions that they see issued for private companies.
37. One respondent from a firm with 6 to 20 partners observed that small businesses are increasingly receiving deficiencies in internal controls because of the inability to prepare financials with appropriate footnotes.
38. A respondent from a firm with 101 to 500 partners felt that GAAP departures dilute the usefulness of financials because such departures allow private companies to pick and choose which standards to comply with.
39. Many of the smaller practitioners stated that their clients prepare financial statements under an OCBOA method. One practitioner from a firm with fewer than 5 partners that provide statements on the income tax basis noted that “our firm quit providing our clients and their lenders and owners GAAP statement over ten years ago. We could not justify the cost of compliance to these standards for the benefits received.”

Standard-setting process

40. Many CPA practitioners felt that the standard-setting process has historically been driven by the needs of public companies. Many of the CPA practitioners with fewer than 5 partners felt that some recent standards are perceived as being reactionary measures borne from emergencies, political pressures, and fraud.
41. Some responses from CPA practitioners cited concerns about the responsiveness of the standard-setting process to the needs of private companies. One respondent from a CPA firm with fewer than 5 partners noted that there is a perception that the input that private companies provide is not taken seriously, and that the time and effort spent on that endeavor is wasted. Other respondents felt that the standard-setting process is overly focused on the perceived needs of users of large public company financial statements. One respondent from a firm with 6 to 20 partners suggested that the voluntary nature of the comment process does not capture the needs of small companies.
42. A CPA firm with over 500 partners felt that:

“...[a] board composed of accounting experts whose experience and dedication is primarily to meet the objectives of preparers, auditors, and users of the financial statements of publicly accountable entities is likely not the best choice for setting standards for private companies that are less focused on capital allocation decisions and more concerned with meeting the needs of a broad range of users in a cost-effective manner.”
43. One trade organization stated that issues and concerns about the standard setters has been a growing issue and hit a “tipping point” when the FASB voted against the work of the PCFRC relative to the release of FIN 48 and FIN 46R.

Question 3b: Are those issues or concerns confined to one or more specific standards, or are they more systemic?

44. The overwhelming majority of the respondents felt the issues or concerns were systemic. Approximately 60% of the respondents cited certain accounting issues as being most problematic. Over half of those respondents had specific concerns regarding income taxes/uncertain tax positions, variable-interest entities, and fair value. Other accounting issues cited included derivatives and other financial instruments, stock compensation, straight-lining of leases, comprehensive income, business combinations, and the proposed lease and revenue recognition standards. In addition to the problematic standards, the majority of the respondents felt the issues were systemic due to the broad-based issues such as the increase in complexity, the pace of change of U.S. GAAP, the increase in qualified or exception-based GAAP opinions, the number of companies reporting under OCBOA, and compliance costs as mentioned above.

Question 3c: Do you believe that those issues or concerns are largely confined to private companies, or are they broader? Please be as specific as possible in your answers.

45. There were varying responses regarding whether the issues or concerns were largely confined to private companies. Many respondents did not respond directly to this question or indicated that they were not able to judge whether the issues were broader because they only deal with private companies. Many respondents suggested that the issues and concerns were broader and also applied to public companies. However, many of those respondents felt that public companies have more resources to deal with the problems. Some of the respondents indicated that the issues also apply to smaller public companies, in particular, because, similar to many private companies, they tend to have limited company resources. One trade organization stated that complexity is a problem for all, but “public companies enjoy access to public capital as a benefit. Private companies and their users do not receive the benefits but have the same costs.”

Question 4: What short-term and/or long-term actions do you believe are necessary to address those issues or concerns? Please be as specific as possible in your answer, and explain your reasoning.

Short-term actions

46. CPA practitioners with fewer than 5 partners generally felt there is some urgency in the need to take action. With regard to proposed new accounting standards, these respondents felt that there should be increased education and awareness about the proposals, specifically targeting private companies. Some suggested webcasts, educational publications, and field tests to fully gauge the real-world impact of new standards on private company stakeholders. One respondent from a CPA firm with 6 to 20 partners felt that the FASB should specifically seek commentary and feedback

- from creditors and creditors' organizations. Respondents also expressed the need for delayed effective dates and longer implementation periods on the new standards.
47. CPA practitioners with over 500 partners generally echoed the sentiments that the FASB should seek more input from private companies during the standard-setting process. One respondent suggested developing a standardized method of collecting and considering views from private company constituents to capture their perspective during the deliberations of each new standard. Additionally, one respondent added that the FASB could strive to provide clearer explanations in the basis for conclusions section of new standards.
 48. One CPA firm with over 500 partners also felt that, going forward, an effort should be made to ensure that new standards are more easily understood by all companies. Moreover, practical expedients for private companies should be considered, and disclosure requirements should be scaled to be appropriate for the primary users of private company financial statements.
 49. A lender responded stating that one short-term solution would be to slow the current pace of standard-setting activities, allowing more private companies to stay current with and participate in the process.
 50. With regard to existing standards, CPA practitioners with fewer than 5 partners felt that there should be more willingness by the FASB to provide private companies with exceptions to specific standards. Firms with 6 to 20 partners felt similarly, stating that there should be exemptions from standards that do not benefit the assessment of essential operations. One respondent from a firm with 6 to 20 partners suggested that standards that have been identified as having questionable relevance to the users of private company financial statements should be immediately suspended and a cost-benefit analysis performed. One respondent proposed forming a coalition of creditor users and those engaged in the standard-setting process to identify areas of the accounting literature in which the needs of creditor users and equity investors differ. This analysis would be performed first on the conceptual framework and second on a standard-by-standard basis.
 51. A chief financial officer similarly requested that more exemptions be allowed for private companies. This respondent felt that the problems with some standards, for example fair value, warranted differences in recognition and measurement.
 52. Other respondents also supported exemptions from certain standards, specifically those that did not focus on cash inflows and outflows. Another suggestion was a simplified checklist format for disclosures, with an emphasis on understandability and use of non-technical language.
 53. CPA firms with over 500 partners generally indicated that, in some cases, relevance and cost-benefit concerns might warrant differences in effective date, transition, and disclosure requirements for private companies. One firm noted that reduced disclosures may be appropriate if it can be shown that users can obtain any incremental information they might need directly from management.
 54. Others suggested that the FASB suspend all proposed standards for private companies until a definitive resolution is determined by the FAF.

Long-term actions

55. Respondents discussed a wide variety of possible long-term actions. Several CPA firms with fewer than 5 partners advocated a separate board devoted to developing standards for private companies. One respondent stated that such a board should be made up of CPAs from regional firms, who would better understand closely held companies. Another respondent advocated for differential reporting and regulatory standards based on size rather than filing status.
56. One response from a CPA practitioner with 21 to 100 partners supported an approach in which the standards issued up to a certain date would be retained for use by private companies. Going forward, each new standard promulgated for public companies would be evaluated for its relevance to private companies. All private companies would retain the option of reporting under full public company standards. Thus, the market would essentially determine which set of standards a private company would report under.
57. Another respondent from a CPA firm with 6 to 20 partners shared a similar idea. This respondent stated that banks were the primary users of private company financial statements. As such, they would ultimately determine the standard setter and level of reporting that is appropriate to meet their needs.
58. Several CPA firms with over 500 partners felt that any substantial recommendations by the Panel might be premature in light of the SEC's forthcoming decision regarding IFRS for public companies. Although the SEC's actions would only directly affect public companies, there would be ramifications for private companies as well. Actions by the Panel may result in unnecessary confusion and complication.
59. Another practitioner with over 500 partners stated that the Disclosure Framework and Conceptual Framework projects should consider the needs of private companies in their goal to create meaningful and effective financial statement disclosures. This respondent also recommended performing some research to help determine whether there were disclosures that could be easily eliminated for private companies.
60. Another respondent from a CPA firm with over 500 partners had a similar suggestion to perform research in order to determine how best to meet the different needs of users of private company financial statements. However, this respondent discussed changes beyond disclosures and into possible differences in recognition and measurement.
61. Another possibility presented was utilizing special-purpose reports to fulfill the diverse needs of users when the use of audited GAAP financial statements is limited.
62. One respondent from a CPA firm with over 500 partners presented several alternative solutions to consider. The first possibility was establishing two distinct standard-setting boards, one to focus on standards for publicly accountable entities and another to focus on the reporting objectives of private companies. The second possibility was creating two boards that had some level of overlapping membership in order to foster collaboration and maintain some consistency. The third possibility was retaining one standard-setting board but creating a subsidiary board to focus on issues relating to private company and not-for-profit entity issues. Respondents from this group also noted that with any of these potential solutions, there would be a need for increased funding and education.

63. Responses from preparers generally indicated that substantial changes were desired. They felt that the lack of relevance of certain standards justified differences not only in disclosure but in recognition and measurement as well. One respondent also had specific concerns about the current cash flow statement. This respondent recommended examining whether the statement was providing value to users in its current form.
64. A response from a state CPA society concurred that some distinction was needed between the reporting for public and private companies. Another state society felt that preparing financial statements on the tax basis was a practical solution to the relevance issue. However, this state society also noted that more guidance was necessary to support using the tax basis as OCBOA.
65. Other respondents had some differing views. Some felt that developing a new set of standards would introduce unnecessary complications since private companies already have the choice of reporting under other comprehensive bases of accounting. On top of that, the complexity of an additional set of GAAP would have implications for academia and practice.
66. Alternatively, a respondent felt that the existing accounting literature should undergo a full relevance review with the perspective of private company concerns.
67. There were other mixed reviews about whether a separate board should set private company standards. One CPA practitioner suggested a practitioner board composed of small to medium firms should set private company GAAP. Another practitioner felt that the separation of standards was long overdue and that a separate private company board made up of users, preparers, and issuers of private companies should set those standards.
68. Another practitioner felt that any attempt to revise U.S. GAAP for private companies would not be successful without a related revision to the framework. This practitioner shared similar views to other practitioners that private companies should have a greater representation in the standard-setting process.

Question 5a: To what extent, if any, would an SEC requirement for public companies to adopt IFRS at a date certain affect your answers above? Why?

IFRS

69. Some respondents felt that while a separate set of standards might be desirable, the SEC decision to require public companies to adopt IFRS should be made first. Some felt IFRS for SMEs would be a viable option. Some of these respondents felt that the Panel may have been too hasty in rejecting IFRS for SMEs.
70. CPA practitioners had widely differing views on IFRS and the role that it might play in financial reporting for private companies. Some respondents from CPA firms with fewer than 5 partners found that their clients did not have a great concern for or awareness of IFRS broadly and IFRS for SMEs. They indicated that many small firms simply do not care and feel that IFRS is irrelevant for companies that do not have significant international operations. One respondent from a CPA firm with 6 to 20 partners agreed that IFRS should not be mandatory for private companies that do not have international investors.

71. On the other hand, a CPA practitioner with 6 to 20 partners observed that its clients were increasingly engaging in international transactions.
72. Some CPA practitioners with fewer than 5 partners felt that the move toward IFRS in the realm of public companies would have a trickle-down effect on private companies in the U.S. Some of the perceived consequences of this trickle-down effect would be increased complexity and limited comparability, increased costs for conversion, and division of the talent pool.
73. Still other respondents felt that private company financial reporting could benefit from a shift toward IFRS. IFRS for SMEs was developed to address the differing reporting needs of private companies. One respondent felt that a move toward a single global standard and worldwide comparability is a positive step.
74. A respondent from a CPA firm with over 500 partners shared a similar sentiment, noting that IFRS for SMEs could be used as a starting point for developing any differential standards for private companies or not-for-profit entities. The respondent maintained that this could help to provide some timely relief for private companies while mitigating some of the risk of diverging too greatly if financial reporting for public companies in the U.S. moves towards IFRS.
75. A preparer expressed concerns about inconsistent application and the subjectivity involved in the more principles-based international standards. Another respondent, however, felt that the principles-based approach could help to address the overwhelming complexity of the current rules.
76. One respondent also noted that a move towards IFRS could increase companies' exposure to international interests, potentially opening up new commercial opportunities.
77. Some respondents feel that IFRS for SMEs was created for very small companies and for developing nations that lack much accounting structure.
78. Another respondent indicated that the future of accounting of private companies affects not only the U.S. It is an issue in Europe and the rest of the world as a growing number of countries are moving toward IFRS.

Question 5b: To what extent, if any, would other outside factors affect your answers above? Which factors and why?

79. Some commented that the needs of users could have an impact on their answers. Another respondent felt that users would be practical about the financial information they would be willing to accept. Other respondents stated that if users started to require IFRS statements, some of their answers would change.
80. Another respondent suggested that the biggest outside factor is the income tax system.

Question 6: Is there any other input that you'd like to convey to the Panel?

81. Some CPA practitioners had general concerns regarding comparability if the Panel were to recommend going to two separate standards. One CPA practitioner with 6 to 20 partners stated that "many new pronouncements appear to be geared toward the complex transactions of the public filers. That all being stated, I have some angst

- with respect to the impact two sets of standards might have, given that two sets of standards would clearly mean differences in comparability of a public company versus a private company, both of which might also operate internationally. I'm unsure how analysts, investors, creditors and other would assess the differences, or what impact those differences might have on such things as the cost of financing, investor confidence and our financial markets.”
82. One practitioner felt that two sets of standards would appropriately address the problems but most standards should remain the same for comparability issues. The practitioner believes that standard setters should try to fix the main issues for private companies but leave the majority of the standards the same.
 83. One practitioner with 6 to 20 partners felt that there was a benefit to retaining consistency between the financials for private and public companies, but that some relief was necessary. The practitioner suggested retaining a single set of accounting literature but varying the degree of application for public and private companies; in this way, there would be consistency across accounting principles, with flexibility in application.
 84. One trade organization felt that a more principles-based approach could also decrease comparability among companies.
 85. Some respondents felt that the standard setters should keep the economics of implementation in mind.
 86. Some respondents were concerned about the proposed leasing standard. One CPA practitioner was concerned that putting leases on the balance sheet would not improve the value of financial statements and would overcomplicate and confuse users. Another practitioner maintained that CFOs and banks need to know the true cash impact of leases as approximated by Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA). If nearly all operating leases become capital leases, interest and depreciation associated with the capital leases will be added back to EBITDA calculations resulting in the illusion that these leases do not impact EBITDA.
 87. One trade organization felt that the cost of capital is another part of the problem. Companies without audited financial statements or without clean opinions pay more for capital.

Questions 7: Do these responses represent your individual views or are they submitted to represent the views of the organization with which you are associated?

88. Many respondents indicated that their response represented their individual views and many indicated their response represented the view of their particular organization. It appeared that the larger the CPA practitioner the individual represented, the more likely he or she responded as an organization.

APPENDIX H

Models and Structures Considered

The staff prepared public meeting handouts to facilitate the audience's understanding of the issues being discussed by the Blue-Ribbon Panel during its July 19, 2010 and October 8, 2010 meetings on alternative standard-setting models and structures for U.S. private companies. This appendix contains portions of those handouts.

“Blue-Ribbon Panel” on Standard Setting for Private Companies Third Meeting (July 19, 2010): Alternative Standards/Standard-Setting Models and Structures for U.S. Private Companies

Based on what the “Blue-Ribbon Panel” (the Panel) has heard at its first two meetings, there appear to be broad-based concerns among private company stakeholders, especially preparers and practitioners, with the current standard-setting system (especially some of the resulting standards). In this meeting, we will focus primarily on various alternative models and structures for standard setting for private companies.

The discussion of models will focus on what type of standards and standard-setting process will best facilitate financial reporting that will meet the needs of users of private company financial statements in a manner that is cost-beneficial for private company preparers, practitioners, users, and others in the financial system. The models are as follows:

U.S. GAAP-BASED/ “HOMEGROWN” MODELS:

Model 1 – U.S. GAAP with Exclusions for Private Companies – current system

Model 2 – U.S. GAAP with Exclusions for Private Companies – with enhancements

Model 3 – U.S. GAAP—Baseline GAAP with Public Company Add-Ons

Model 4 – Separate, Standalone GAAP Based on Current U.S. GAAP (the “Canadian” Approach)

Model 5 – Separate, Standalone GAAP from the Ground up Based on New Framework

IFRS-BASED MODELS:

Model 6 – Unmodified IFRS for SMEs

Model 7 – IFRS for SMEs Customized (“Americanized”) for U.S. Private Companies

Many of these models, which are briefly described in the Appendix, build upon work performed by the Private Company Financial Reporting Committee (PCFRC) and other organizations. Most of the models contemplate the creation and/or use of some sort of private company conceptual framework. The models represent two continua, one based on U.S. GAAP and another based on IFRS. Along these continua, the model that the Panel ultimately homes in on may actually combine features of more than one of the models. Or, the Panel might home in on a succession of models, one shorter-term and potentially another longer-term—if, for example, the ultimate model would take a long time to achieve or if the choice of an ultimate model is viewed as somewhat dependent on outside factors, such as the SEC’s decision regarding whether and how to adopt/incorporate IFRS for public companies.

In its discussion of models, the Panel will weigh the pros and cons of the models, both in the specific context of the private company sector and the broader context of the financial reporting system as a whole.

The Panel will also discuss various possible structures for the standard-setting board (and related resources, such as advisory groups), perhaps the key driver in achieving the desired model(s). These structures are arrayed along the following two continua:

STRUCTURES FOR U.S. GAAP-BASED/ HOMETGROWN MODELS:

Structure A – Current FASB Board

Structure B – Restructured FASB Board (with greater private company representation)

Structure C – New, Separate Private Company Standards Board

STRUCTURES FOR IFRS-BASED MODELS:

Structure D – IASB Board

Structure E – Board Structure for Customized IFRS for SMEs (in addition to IASB Board)

i) Current FASB Board

ii) Restructured FASB Board

iii) New, Separate Private Company Standards Board

As with the models, the Panel could ultimately home in on only certain elements of the structure, on a combination of structures, or on an evolutionary series of structures.

APPENDIX: MODELS

Model 1 – U.S. GAAP with Exclusions for Private Companies – current system

- Current U.S. GAAP (the Codification) would be used by all companies and improved as necessary through the FASB’s regular standard-setting activities.
- Those activities utilize the current FASB Nonpublic Entity staff (Assistant Director, Project Manager, Postgraduate Technical Assistant), who work with the FASB project staff and the FASB board in a close, consultative capacity (leading to explicit consideration of private company issues and feedback, documented in the Basis for Conclusions section of all proposed and final Accounting Standards Updates), and with the PCFRC and FASB’s Small Business Advisory Committee in their current advisory roles.
- Differences (exclusions) for private companies would continue to be determined on a standard-by-standard basis.
- This model would not contemplate the creation of a separate conceptual framework for private companies.
- However, a project to simplify standards, especially in the area of disclosures, could be undertaken for all entities (private and public), perhaps in connection with the FASB’s Disclosure Framework Project.

Model 2 – U.S. GAAP with Exclusions for Private Companies – with enhancements

- Current U.S. GAAP (the Codification) would be used by all companies and improved as necessary through the FASB’s regular standard-setting activities.
- Differences (exclusions) for private companies would continue to be determined on a standard-by-standard basis.
- A conceptual framework for private companies would be created to serve as a basis for making exceptions. Such a framework would be based on user needs but would be modest (approximately on the level of the “Concepts and Pervasive Principles” chapter that the IASB put into the IFRS for SMEs document).
- Various other enhancements could be made, such as to board structure, staffing, and other elements of standard-setting. For example, the FASB could be expanded to include a member with small, private company experience. Together with the private company conceptual framework, these enhancements might further ensure that appropriate and adequate focus is placed on private company issues, with resulting differences for private companies.

Model 3 – U.S. GAAP—Baseline GAAP with Public Company Add-Ons

- Current (existing) U.S. GAAP (the Codification) would be reviewed and reorganized into a baseline GAAP for all entities, based on user needs, and with additional GAAP requirements (“add-ons”) for public companies.

- The approach to standards currently under development could be changed to establish a baseline standard for all entities and additional requirements for public companies even before completion of the overall baseline separation project.
- This model contemplates the need to create a separate conceptual framework for private companies, or to reexamine/revise the existing conceptual framework, to serve as a basis for making decisions as to what to put in the baseline. If separate, such framework would be modest (approximately on the level of the “Concepts and Pervasive Principles” chapter that the IASB put into the IFRS for SMEs document).

Model 4 – Separate, Standalone GAAP Based on Current U.S. GAAP (the “Canadian” Approach)

- Current U.S. GAAP would be reviewed, modified, and developed into a comprehensive and self-contained set of accounting standards for private companies.
- This approach contemplates a major overhaul project to review and significantly streamline current U.S. GAAP, as well as ongoing activities to update but keep simplified (similar to what the IASB and the Canadian AcSB will be doing with their respective private company standards).
- This model contemplates the need to first create a conceptual framework for private companies that would serve as a yardstick for making streamlining and other simplification decisions. Such a framework would be modest (approximately on the level of the “Concepts and Pervasive Principles” chapter that the IASB put into the IFRS for SMEs document).

Model 5 – Separate, Standalone GAAP from the Ground up Based on New Framework

- This model is focused solely on the private company sector and begins with the creation of a new private company conceptual framework based on private company user needs. As opposed to the private company framework described in Models 2–4, which could be described as a “differential framework,” the framework would be from the ground up, entail a major project to create, and could be significantly different from the current GAAP conceptual framework (including revisions currently being contemplated by the FASB and IASB). The model framework suggested in the draft white paper released by FEI’s Committee on Private Companies-Standards (the Committee) is an example of this type of framework.
- A comprehensive set of standards would be developed based on this new framework and would then constitute a separate, self contained set of standards for use by private companies.

Model 6 – Unmodified IFRS for SMEs

- This models would use IFRS for SMEs as it exists today
- IFRS for SMEs, as promulgated by the IASB, is not intended for entities that have public accountability (e.g., financial institutions).
 - Part of a possible recommendation of IFRS for SMEs could be a recommendation about whether IFRS for SMEs should be permitted to be used

- by private companies with public accountability. (However, if used by such entities, they would not technically be able to refer to such standards as IFRS for SMEs.)
- IFRS for SMEs includes a group of Concepts and Pervasive Principles that serve as a framework for the simplifications made from full IFRS.

Model 7 – IFRS for SMEs Customized (“Americanized”) for U.S. Private Companies

- The IFRS for SMEs standards would be tailored to suit the needs of private company stakeholders in the U.S.
- This model contemplates an initial project to review and modify IFRS for SMEs as appropriate, possibly significantly. (However, depending on the nature and extent of the modifications, we might not actually be able to refer to the resulting standards as IFRS for SMEs.)
- Ongoing decisions would be required to elect to accept IASB revisions to the SME document verbatim or elect to modify them for U.S. private companies.

“Blue-Ribbon” Panel on Standard Setting for Private Companies Fourth Meeting (October 8, 2010): Discussion of Standard-Setting Models and Structures (cont’d), Recommendations

In this meeting, the “Blue-Ribbon” Panel (the Panel) will continue its discussion and debate on alternatives to the current standard-setting system. At its July 19, 2010 meeting, there was wide agreement among Panel members that:

- The status quo is unacceptable
- U.S. private companies should not be leading the charge, *en masse*, to an IFRS-based set of standards in advance of a potential move by U.S. public companies

Accordingly, the Panel asked staff to make refinements to the following set of U.S. GAAP-based standard-setting models discussed at the July 19 meeting:

Model 2 – GAAP with exceptions for private companies

Model 3 – Baseline GAAP with add-ons for public companies

Model 4 – Separate, standalone GAAP for private companies

For Models 2 and 4, the staff also outlined two structural variations, one featuring a **restructured FASB** (Models **2A** and **4A**) and the other featuring a **separate private company board** (Models **2B** and **4B**). Because of the nature of Model 3, only a version with a single standard-setting board for both public and private companies (a restructured FASB) is feasible, so only one refined version of that model has been outlined. The outline of the five models is contained in the pages that follow.

After discussing a summary of responses received in connection with the Panel’s call for written public submissions—with a focus on any new information—the Panel will proceed with the discussion and debate of the models. The Panel’s aim will be to reach a substantial consensus among Panel members as to which model to recommend to the FAF Board of Trustees as being in the best long-term interest of users of financial statements of U.S. private companies within the broader context of the overall U.S. financial reporting system.

Because the models represent points along a continuum of possible models, the Panel could recommend a hybrid model. And, because the models will take a period of time to fully achieve, with the length of time varying somewhat among the models, the Panel could recommend an evolutionary sequence of models, and/or some additional shorter-term actions by the FAF and/or the FASB.

Blue-Ribbon Panel Model Outline

Based on what we heard at the last meeting, the staff has narrowed the alternatives to three possible models, with structural variations for two of those models, to bring forward for discussion at the October 8th meeting. As with the first round of models and structures, the models and structural variations outlined here are meant simply as a starting point for discussion. The model that the Panel ultimately homes in on may actually combine features of more than one of the models, or the Panel might recommend something in-between models. Please also note that, in this round of models, the staff has avoided speculating within the models about what recognition, measurement, disclosure, or presentation differences could occur, since the standard setter will ultimately determine those differences.

In reviewing the models, the Panel should consider what short-term and long-term changes may need to be made to be able ultimately to achieve the respective models. The most effective approach to accomplish the desired end-state model could well be a succession (evolution) of models.

Overview of Models and Structures

In the pages that follow, we present the following models/structures:

Model 2A – GAAP with exceptions for private companies (enhanced) with restructured FASB Board

Model 2B – GAAP with exceptions for private companies (enhanced) with separate private company standards board

Model 3A – Baseline GAAP with add-ons for public companies with restructured FASB Board

Model 4A – Separate, standalone GAAP for private companies with restructured FASB Board

Model 4B – Separate, standalone GAAP for private companies with separate private company standards board

MODELS: U.S. GAAP-Based			
STRUC TURES	2 GAAP with exceptions for private companies, enhancements to current model	3 Baseline GAAP with add-ons for public companies	4 Separate, standalone GAAP for private companies
A) Restructured FASB Board	<p style="text-align: center;"><u>MODEL 2A</u></p> <p>Description:</p> <ul style="list-style-type: none"> Current U.S. GAAP (the Codification) would be used by all companies and continue to be improved as necessary through an exception-based standard-setting process, with specific enhancements as discussed below. A restructured FASB would act as the standard setter. <p>Framework:</p> <ul style="list-style-type: none"> The current conceptual framework would be examined and augmented as necessary to include a differential framework, which would serve as a basis for making decisions about what is appropriate for private company exclusions. 	<p style="text-align: center;"><u>MODEL 3A</u></p> <p>Description:</p> <ul style="list-style-type: none"> Current U.S. GAAP (the Codification) would be reviewed and reorganized into a baseline GAAP for all entities, based on user needs, and with additional GAAP requirements (“add-ons”) for public companies, and continue to be improved as necessary through a standard-setting process based on that split. A restructured FASB would act as the standard setter. <p>Framework:</p> <ul style="list-style-type: none"> The current conceptual framework would be examined and augmented as necessary to include a differential framework, which would serve as a basis for making decisions about what is the appropriate baseline for all companies and what are appropriate as add-ons for public companies. 	<p style="text-align: center;"><u>MODEL 4A</u></p> <p>Description:</p> <ul style="list-style-type: none"> Current U.S. GAAP (the Codification) would be reviewed, modified, and developed into a simplified, self-contained set of accounting standards for private companies, which would then be improved as necessary on a periodic basis. A restructured FASB would act as the standard setter. <p>Framework:</p> <ul style="list-style-type: none"> The current conceptual framework would be examined and augmented as necessary to include a differential framework, which would serve as a basis for making streamlining and other simplification decisions.

MODELS: U.S. GAAP-Based			
STRUC TURES	2 GAAP with exceptions for private companies, enhancements to current model	3 Baseline GAAP with add-ons for public companies	4 Separate, standalone GAAP for private companies
	<u>MODEL 2A—continued</u>	<u>MODEL 3A—continued</u>	<u>MODEL 4A—continued</u>
	<p>Boards:</p> <ul style="list-style-type: none"> • In the expansion of the FASB back to seven members and perhaps ultimately more, the FAF should assess the FASB’s composition and adjust as necessary to include sufficient private company experience and perspective. In connection with this, the FAF should consider appointing one or more members whose experience is primarily with the private company sector. • Assess and adjust the FAF’s composition as necessary to ensure its oversight function has the appropriate private company experience and perspective. • Assess and adjust Financial Accounting Standards Advisory Council (FASAC) composition as necessary to ensure its advisory function has the appropriate private company experience and perspective. (FASAC is FASB’s primary advisory group.) 	<p>Boards:</p> <ul style="list-style-type: none"> • In the expansion of the FASB back to seven members and perhaps ultimately more, the FAF should assess the FASB’s composition and adjust as necessary to include sufficient private company experience and perspective. In connection with this, the FAF should consider appointing one or more members whose experience is primarily with the private company sector. • Assess and adjust the FAF’s composition as necessary to ensure its oversight function has the appropriate private company experience and perspective. • Assess and adjust Financial Accounting Standards Advisory Council (FASAC) composition as necessary to ensure its advisory function has the appropriate private company experience and perspective. (FASAC is FASB’s primary advisory group.) 	<p>Boards:</p> <ul style="list-style-type: none"> • In the expansion of the FASB back to seven members and perhaps ultimately more, the FAF should assess the FASB’s composition and adjust as necessary to include sufficient private company experience and perspective. In connection with this, the FAF should consider appointing one or more members whose experience is primarily with the private company sector. • Assess and adjust the FAF’s composition as necessary to ensure its oversight function has the appropriate private company experience and perspective. • Assess and adjust Financial Accounting Standards Advisory Council (FASAC) composition as necessary to ensure its advisory function has the appropriate private company experience and perspective. (FASAC is FASB’s primary advisory group.)

MODELS: U.S. GAAP-Based			
STRUC TURES	2 GAAP with exceptions for private companies, enhancements to current model	3 Baseline GAAP with add-ons for public companies	4 Separate, standalone GAAP for private companies
B) New Separate Private Company Standards Board	<p style="text-align: center;"><u>MODEL 2B</u></p> <p>Description:</p> <ul style="list-style-type: none"> Current U.S. GAAP (the Codification) would be used by all companies and continue to be improved as necessary through an exception-based standard-setting process, with specific enhancements as discussed below. This model would contemplate a new, separate private company standards board under the FAF—see board section. <p>Framework:</p> <ul style="list-style-type: none"> The current conceptual framework would be examined and augmented as necessary to include a differential framework, which would serve as a basis for making decisions about what is appropriate for private company exclusions. 	<p>A separate, private company standard-setting board under a baseline GAAP model would not be feasible.</p>	<p style="text-align: center;"><u>MODEL 4B</u></p> <p>Description:</p> <ul style="list-style-type: none"> Current U.S. GAAP would be reviewed, modified and developed into a simplified and self-contained set of accounting standards for private companies, which would then be improved as necessary on a periodic basis. This model would contemplate a new, separate private company standards board under the FAF—see board section. <p>Framework:</p> <ul style="list-style-type: none"> The current conceptual framework would be examined and augmented as necessary to include a differential framework, which would serve as a basis for making streamlining and other simplification decisions. Alternatively, a separate, robust conceptual framework specifically geared to private companies could be created to help the board develop a “from the ground up” private company GAAP. (This was described as model 5 in the previous model write-up.)

MODELS: U.S. GAAP-Based			
STRUC TURES	2 GAAP with exceptions for private companies, enhancements to current model	3 Baseline GAAP with add-ons for public companies	4 Separate, standalone GAAP for private companies
	<p><u>MODEL 2B—continued</u> Boards:</p> <ul style="list-style-type: none"> • Separate private company standard-setting board that follows the work of the FASB. The private company board would be empowered to review both proposed standards and existing standards that the FASB sets and determine whether to make exceptions or modifications for private companies. • Assess and adjust the FAF’s composition as necessary to ensure its oversight function has the appropriate private company experience and perspective. • The new standard-setting board would need new primary advisory group in lieu of FASAC. 		<p><u>MODEL 4B—continued</u> Boards:</p> <ul style="list-style-type: none"> • The board under this model would be the standard setter for the separate, standalone GAAP for private companies. • Assess and adjust the FAF’s composition as necessary to ensure its oversight function has the appropriate private company experience and perspective. • The new standard-setting board would need new primary advisory group in lieu of FASAC.