AICPA® PCPS
Private Companies Practice Section

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Technical Issues Alert

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

# TIC Discusses Standards and Proposals with the FASB and PCC

TIC maintains strong ties to standard setters, sharing the committee's perspectives on the issues that affect private companies and making recommendations to enhance standards in development. Here are some of the issues discussed at TIC's most recent meetings with the FASB and the PCC.

*Applying VIE Guidance to Entities Under Common Control.* Given diversity in practice and other concerns, the PCC has urgently recommended that the FASB undertake a project dealing with issues not already addressed in ASU 2014-07, *Consolidation (Topic 810): Applying Variable Interest Entities Guidance to Common Control Leasing Arrangements*. The additional project has been added to the FASB's research agenda, along with a related project to reconsider the organization and format of Topic 810. The FASB, the PCC and TIC discussed some alternative proposals to address the issues. TIC members generally agreed that a scope exception for applying the VIE guidance in Topic 810, including the determination of whether a private company under common control is a VIE, was needed for private entities. They discussed approaches to providing one, along with ideas for preventing potential structuring of transactions to circumvent guidance.

In the meantime, the FASB issued an exposure draft, *Consolidation: Interests Held through Related Parties That Are under Common Control*, which TIC supports to address a question raised during the implementation of ASU 2015-02, *Consolidation (Topic 810): Amendments to the Consolidation Analysis.* Specifically, if a reporting entity is the single decision maker of a variable interest entity, the amendments in this proposed Update would require that reporting entity to include all of its direct variable interests in a VIE and, on a proportionate basis, its indirect variable interests in a VIE held through related parties to determine whether it is the primary beneficiary of that VIE. This evaluation would include all related parties as defined in paragraph 810-10-25-43, including those under common control with the single decision maker.

*Simplifying the Balance Sheet Classification of Debt*. TIC members described their concerns about the proposed balance sheet classification changes for short-term debt that is refinanced on a long-term basis after the balance sheet date but before financial statement issuance (or for a private company, when financial statements are available to be issued). Under current standards, refinanced debt that meets certain conditions is classified as a long-term liability, but under the board's proposal, it would be classified as a current liability. Instead, TIC recommended that the board focus on targeted improvements, as discussed in a related PCC agenda paper.

*Share-Based Payment Disclosures and Deferred Tax Assets for Underwater Options under ASC Topic 718: Compensation—Stock Compensation.* TIC strongly supports a potential exemption from certain disclosures for private entities (see separate article in this issue for more details). TIC members summarized their concerns, including the disclosures' lack of relevance for private entities and unnecessary cost and complexity. Separately, TIC recommended that the board reconsider the accounting for deferred tax assets on underwater options. Currently, these assets must remain on the books even if there is no possibility that the options to which they relate will be exercised.

*Equity Method Simplification for Private Entities.* TIC recommended that the board undertake a project focusing on simplifications for accounting for basis differences, which can be a challenge for non-public entities. TIC discussed inconsistencies that committee members have seen in practice and suggested possible simplifications.

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**FUTURE MEETINGS**

TIC meetings offer local practitioners the chance to provide their unique perspectives in the standard-setting process. All CPAs are invited to attend. Contact Kristy Illuzzi, CPA, TIC Staff Liaison, at the AICPA at (919) 402-4057 to learn about attending or receiving information on upcoming meetings.

The next TIC meetings will be held:

- November 15 and 16, San Antonio, TX (TIC's annual liaison meeting with ARSC)
- January 10 and 11, Fort Lauderdale, FL (TIC's annual liaison with the ASB)
- May 4 and 5, Washington, DC (TIC liaison with PCPS Executive Committee)

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

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Other FASB proposals of note include:

- *Not-for-Profit Entities–Consolidation (Subtopic 958-810): Clarifying When a Not-for-Profit Entity That Is a General Partner Should Consolidate a For-Profit Limited Partnership or Similar Entity*. TIC generally supported this proposal, which is restoring some guidance from a superseded ASU. It will not add new language or guidance, but will offer clarifications on when not-for-profits can apply the fair value option. TIC did note that the ED inadvertently eliminates some not-for-profits' ability (once ASU 2016-01 is effective) to carry investments, over which they have significant influence or a controlling financial interest, at fair value under the portfolio-wide alternative, rather than using the equity method or consolidating, respectively.

- A proposed FASB ASU, *Income Taxes (Topic 740): Disclosure Framework—Changes to the Disclosure Requirements for Income Taxes*. Practitioners can turn to a FASB in Focus and Decision Questions Considered in Establishing Disclosure Requirements for more information. In its comment letter on the ED, TIC supported the proposed amendments and asked the board to consider an additional amendment to the disclosures regarding unrecognized tax benefits that would clarify that disclosure of open tax years that remain subject to examination by major tax jurisdictions is unnecessary when no unrecognized tax benefits exist. This is consistent with guidance issued by the Center for Plain English Accounting.

- Proposed Statement of Financial Accounting Concepts—*Concepts Statement 8—Conceptual Framework for Financial Reporting—Chapter 7: Presentation*. The FASB uses its Conceptual Framework for Financial Reporting to develop financial accounting and reporting standards. In a FASB in Focus article on this proposal, the board notes that, "Concepts Statement 5, *Recognition and Measurement in Financial Statements of Business Enterprises*, addresses—among other things—recognition, measurement, and certain concepts for presentation of information on the face of financial statements. The Board concluded that the discussion of presentation could be further developed and improved with the objective of providing a foundation for future standards that enhance financial statement users' abilities to assess prospects for future cash flows by addressing how to:
    - Group individual recognized items into line items and subtotals.
    - Clarify the relationships among an entity's assets, liabilities, and equity, and the effects of related changes of those assets and liabilities on comprehensive income and cash flows."

Comments on this ED are due by November 9. ■

# TIC Meets with FASB Staff

Based on its recent meetings with FASB staff and monitoring of FASB activities, here are proposals or projects in development or news that will have an impact on private entities and their CPAs:

- Proposed ASU, *Technical Corrections and Improvements to Update No. 2014-09, Revenue from Contracts with Customers (Topic 606).* This ED would address nine issues that have arisen when implementing existing guidance, based on feedback from a variety of sources. TIC believes the proposed amendments would resolve the scope issue, which arose after the issuance of ASU 2014-09, as to the applicable guidance for accounting for preproduction costs relating to long-term supply arrangements. However, the proposed amendments, which would supersede the guidance in Subtopic 340-10 in favor of the guidance within Subtopic 340-40, may have the unintended consequence of deleting valuable guidance within Subtopic 340-10 on certain preproduction costs related to long-term supply arrangements. TIC pointed to one specific example, in paragraphs 340-10-05-6 and 340-10-25-1 through 25-2, involving costs incurred by a manufacturer to perform certain services related to the design and development of products it will sell under long-term supply arrangements and to design and develop molds, dies, and other tools that will be used in producing those products. This guidance has been extremely helpful to preparers who face this accounting issue. TIC also suggested the FASB might want to consider clarifying to what extent an entity should consider costs associated with the renewal and fulfillment of contracts. TIC members also suggested a variety of editorial changes and clarifications.

- Proposed ASU, *Other Income—Gains and Losses from the Derecognition of Nonfinancial Assets (Subtopic 610-20): Clarifying the Scope of Asset Derecognition Guidance and Accounting for Partial Sales of Nonfinancial Assets*. TIC noted the usefulness of a flowchart that is now in the example section, explaining that it would be very valuable in helping preparers understand how aspects of the guidance apply to them. TIC members recommended that the flowchart be included within the scope section of the final document. TIC also discussed the importance of aligning certain principles included in Topic 606 and the effective date of this document with those of planned guidance on clarifying the definition of a business.

- A new, expanded edition of the AICPA alert *Revenue Recognition: Accounting and Auditing Considerations—2016/17* provides a timely update on recent developments related to the FASB's new standard. The alert outlines the provisions under the new framework for revenue

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recognition, illustrating differences from current standards, and also focuses on many of the relevant auditing considerations applicable to revenue.

- The FASB issued ASU 2016-08, *Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations*. **Tip: Practitioners should be aware that principal versus agent considerations would apply to all entities with contracts with customers, including not-for-profits.**

- Other recent standards issued by the FASB include:

  - ASU 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments (a consensus of the Emerging Issues Task Force)*.

  - ASU 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*.

  - ASU 2016-13, *Measurement of Credit Losses on Financial Instruments*. This standard is of particular significance to private entities because its scope includes estimating credit losses on trade receivables, so we have included a link to the full text of the ASU here for reference.

- AICPA Health Care Industry Revenue Recognition Issues. Following the FASB's issuance of ASU 2014-09, *Revenue from Contracts with Customers*, the AICPA formed 16 industry task forces to help develop implementation guides to address significant issues associated with the new standard. The critical issues identified by the health care industry task force included self-pay balances and application of the portfolio approach to patient balances. TIC provided informal feedback to the AICPA Health Care Entities Revenue Recognition Task Force focusing on where additional examples or guidance may be needed.

- The Financial Accounting Foundation, which oversees the FASB and the GASB, has issued its 2015 Annual Report in an enhanced digital format. The new digital edition of the report—"Serving the Financial Statement User"—can be used by any browser in any format, including desktop, tablet or phone. Readers can access the annual report on the go and can quickly navigate different sections. This version includes links to relevant documents issued by the FAF, FASB and GASB. New related videos feature individual financial statement users discussing the importance of high-quality financial reporting to the work that they do. Additional videos highlight how the FASB and the GASB serve the capital markets through their specific roles in the standard-setting process, and how the U.S. GAAP Financial Reporting Taxonomy benefits investors. To access the digital-friendly and PDF versions of the 2015 FAF Annual Report, visit www.accountingfoundation.org/annualreport. ■

# TIC Calls for Simplifications in Share-Based Payment Disclosures

As part of its ongoing communications with standard setters, TIC has recommended that the FASB should exempt private entities from certain required disclosures required under *ASC Topic 718, Compensation—Stock Compensation*. In TIC's own discussions on simplifications regarding recognition, measurement and disclosure of share-based payment transactions, the committee discovered some share-based payment disclosures were causing unwarranted cost and complexity. TIC reviewed the required disclosures for share-based payment awards issued to employees, identified opportunities to simplify or eliminate some that don't provide useful information to users of nonpublic entity financial statements, and shared the committee's observations during the TIC liaison meeting with the FASB.

TIC cited several disclosures that are irrelevant to private companies, including weighted-average exercise prices and the number and weighted-average grant-date fair value (or calculated value for a nonpublic entity that uses that method or intrinsic value for awards measured at that value) of certain equity instruments. ■

# TIC Addresses Issues with the GASB

TIC members met recently with GASB Chair David Vaudt and GASB staff members to discuss a variety of topics.

*Increased Use of Deferred Inflows and Outflows of Resources*. In response to a request from GASB staff, TIC members discussed their experiences with the guidance in this area. They reported that deferred inflows and outflows in general were a particularly difficult concept to explain to their clients or to financial statement users and that more educational resources could alleviate the problem.

*Omnibus 201X*. TIC gathered information on the issues that had driven the issuance of this ED, which includes guidance updates in a number of areas, including blending component units, goodwill, fair value measurement and application and postemployment benefits. Comments are due by November 23.

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*Revenue and Expense Recognition*. In its discussion of this project, TIC noted some of the complexities in implementing the FASB's revenue recognition standard, which is principles based. If the GASB takes a principles-based approach in this project, TIC requested that it offer comprehensive implementation guidance to help governments understand and put the standard to work.

*Financial Reporting Model Update—Reexamination of Statements 34, 35, 37, 41, and 46 and Interpretation 6*. TIC expressed appreciation to the board for taking on this project, which is reexamining existing guidance in a number of GASB statements, and further considering recognition concepts for governmental funds.

*Leases*. GASB staff provided an update on comments received on this ED and on tentative plans for changes to the initial proposal. GASB noted the value of observations in TIC's comment letter and reported that planned revisions included a definition of "biological assets," based on a TIC recommendation. TIC offered further insights into its comments, calling for concise and meaningful note disclosure that will help improve comparability. TIC expressed appreciation for the board's efforts on this project and its redeliberations. (See a separate article in this issue on TIC's participation in a public meeting on this ED.)

*Fiduciary Activities*. TIC reviewed some of its concerns about this ED, which the GASB has been redeliberating. TIC and GASB staff discussed changes to the guidance on student activity funds, which was one of TIC's main concerns.

*TIC Involvement in GASB Projects*. GASB staff thanked TIC for its feedback over the years and TIC members expressed their willingness to be involved in future GASB projects. ■

# TIC Participates in Public Hearing on GASB Leases ED

In its *Leases* ED, the GASB has proposed establishing a single approach for state and local governments to report leases, under the principle that leases are financings of the right to use an underlying asset. Exceptions to the approach include short-term leases (12 months or less) and financed purchases. The ED would cover lease contracts for nonfinancial assets—including vehicles, heavy equipment, and buildings—but not grants, donated assets and leases of intangible assets (such as patents and software licenses).

TIC member Ted Williamson offered the committee's input in a recent public hearing on the ED. Among other areas, he discussed the need to simplify the ED's requirements for determining the lease and service components for lease agreements with multiple components, to clarify what would make a price "readily available" under the guidance, and to further define a "biological asset." He also discussed the need for more guidance on objectives and criteria for aggregating leases for footnote disclosures and requested details on classifying and presenting a right-to-use asset. ■

# Going Concern SAS ED Issued

*The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern*, a recent ED from the ASB, would supersede SAS No. 126, of the same title, and some elements of SAS No. 122, *Statements on Auditing Standards: Clarification and Recodification*, as amended. It comes in response, in part, to the FASB's ASU No. 2014-15, *Presentation of Financial Statements—Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern*, which establishes management's responsibility to evaluate and disclose if there is substantial doubt about an organization's ability to continue as a going concern. It is also driven by the ASB's convergence project with the IAASB.

Among other changes, the ED acknowledges that special purpose financial statements may or may not be prepared in accordance with a financial reporting framework for which the going concern basis of accounting is applicable. If the going concern basis of accounting is applicable in the preparation of financial statements prepared in accordance with a special purpose framework, the ASB proposes that AU-C section 570 applies. Therefore, the auditor should consider whether disclosures about risks and uncertainties would be needed in audits using special purpose frameworks and audits of single financial statements and specific elements, accounts, or items of a financial statement. The final SAS, if approved and issued shortly after the January 2017 ASB meeting, would be effective for audits of financial statements for periods ending on or after December 15, 2017.

TIC generally supported the proposed amendments in this ED and agreed with using International Standard on Auditing 570 [Revised], *Going Concern*, as a base for the ED, to the extent applicable, as well as the proposal's accounting framework neutral approach that would allow the standard to be applicable regardless of the financial accounting framework used in preparing the financial statements. TIC generally approved

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of what it considered the ED's most significant changes, the proposed standards for audits of special purpose frameworks, single financial statements, specific elements, accounts or items of a financial statement and interim financial information. In particular, TIC members expressed appreciation for an example that reminds the auditor that the requirement to consider fair presentation includes an evaluation of whether the financial statements properly disclose the entity's risks and uncertainties. TIC did recommend some revisions to improve clarity and consistency. ■

# ARSC Issues Clarified Standard on Pro Forma Financial Information

In line with its Clarity Project, the AICPA's Accounting and Review Services Committee has completed the clarity redrafting of its last pre-clarity AR section in AICPA *Professional Standards* and issued SSARS No. 22, *Compilation of Pro Forma Financial Information*, to clarify AR section 120, *Compilation of Pro Forma Financial Information* (AICPA, *Professional Standards*). SSARS No. 22 supersedes SSARS No. 14 of the same title, as amended, and becomes effective for compilation reports on pro forma financial information dated on or after May 1, 2017. ■

# Quality Issues in Government and NPO, EBP Audits

The AICPA Professional Ethics Division has compiled a list of quality issues found in its investigations of government and not-for-profit entity audits and in employee benefit plan audits over the last two years.

- The division completed 596 investigations, 145 of which were government and not-for-profit entities. The quality issues it found fell into these categories: Single Audit issues; auditor's reporting; audit procedures; financial statement deficiencies; and other issues.
- 258 investigations involved employee benefit plans. Quality issues found in this area fell into: firm management; auditor's reporting; audit procedures; and financial statement deficiencies.

The division said that when there were reporting, disclosure and auditing errors, it found that the practitioner would have benefited from additional experience and specific continuing professional education in these specialized area. In addition, the errors would have been detected by a quality control review of the financial statements and risk areas.

When quality issues are identified, the member is subject to remediation—such as CPE or pre-issuance reviews of select engagements by an independent third party—and in some instances sanctions that include publication and admonishment, suspension or expulsion from AICPA membership. ■

# Ethics Technical Correction Issued

The Professional Ethics Executive Committee has made a technical correction to the "Unsolicited Financial Interest" interpretation under the "Independence Rule" (AICPA, Professional Standards, ET sec. 1.240.020). The correction elaborates on the definition of the period when a covered member does not participate on the attest engagement team for the purposes of the rule. ■

# Audit and Attest Update

- An ARSC SSARS ED, *Amendment to Statement on Standards for Accounting and Review Services No. 21 Section 90, Review of Financial Statements*, would amend paragraphs .05 and .80–.82 of AR-C section 90, *Review of Financial Statements* (AICPA, *Professional Standards*), and the corresponding application paragraphs, related to reporting on supplementary information that accompanies reviewed financial statements and the accountant's review report thereon. The proposed SSARS is expected to become effective upon issuance. TIC agreed with the proposed changes and decided not to issue a formal comment letter.
- An ASB SAS ED, *Auditor Involvement With Exempt Offering Documents*, proposes specific performance requirements when the auditor is involved with an exempt offering. Although an auditor is not required to become involved in an offering

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document except when the benchmarks defining involvement are met, auditors may become voluntarily involved with an offering document in other circumstances. The proposed SAS would become effective for offering documents with which the auditor is involved that are initially distributed, circulated, or submitted on or after June 15, 2018. TIC welcomed the ED given the current diversity in practice, particularly involving the nature and extent of the procedures that the auditor should perform. TIC generally agreed on the offerings that would be involved and the activities that would trigger auditor involvement. TIC did raise questions about some of the proposed subsequent event guidance, including concerns about the extent of the auditor's responsibilities for the subsequent discovery of facts. TIC submitted its comment letter on October 12.

- E-versions of the AICPA Audit and Accounting Practice Aid, *Establishing and Maintaining a System of Quality Control for a CPA Firm's Accounting and Auditing Practice*, enhance practitioners' abilities to create a firm's quality control system policies and procedures, as required by QC section 10, *A Firm's System of Quality Control* (AICPA, *Professional Standards*). The free 2016 edition of this publication comes in two versions: one for small and medium-sized firms and another for sole practitioners. ■

# COSO Fraud Risk Management Guide Released

Developed by the Committee of Sponsoring Organizations of the Treadway Commission, the *Fraud Risk Management Guide* draws from and updates the 2008 *Managing the Business Risk of Fraud: A Practical Guide* for more recent developments, revises terminology to be consistent with the 2013 Framework, and adds important information related to technology developments—specifically data analytics. This guide can serve as best practices guidance for organizations to follow in addressing this new fraud risk assessment principle; provides implementation guidance that defines principles and points of focus for fraud risk management and describes how organizations of various sizes and types can establish their own Fraud Risk Management Programs; contains references to other sources of guidance to allow for tailoring a Fraud Risk Management Program to a particular industry or to government or not-for-profit organizations; and contains valuable information for users who are implementing a fraud risk management process.■

# Cybersecurity Updates for Practitioners

Cybersecurity risks are a hot topic, everywhere from corporate boardrooms to small businesses. The Internal Revenue Service has warned tax practitioners about a new threat in which hackers take control of computers and file fraudulent returns. Learn more about the new cybersecurity threat in this article in the *Journal of Accountancy* and about other tech threats in this article in *CPA Insider*. ■

# Peer Review EDs and Quality Tips from the *Reviewer Alert*

This section tracks the status of Peer Review Board (PRB) exposure drafts and alerts practitioners to articles from Peer Review's *Reviewer Alert* that offer insights into more effectively performing peer reviews, as well as best practices for enhancing audit quality.

- Exposure Drafts:
  - The AICPA Peer Review Board has proposed modifying the representation letter to reflect all engagements that must be selected in a review, including Single Audits. The peer review report must also specifically state that Single Audits have been selected and reviewed. The proposed revisions would become effective for reviews beginning on or after Jan. 1, 2017. TIC agreed with the proposed changes and decided not to issue a formal comment letter. This exposure draft will be presented to the PRB for approval during the November 14 Open Session PRB Meeting.
  - The PRB has approved the changes proposed in its ED on *Allowing Firms with No AICPA Members to Enroll in the AICPA Peer Review Program*, at its September 27 Open Session meeting. The revisions allow firms with no AICPA members to enroll in the Peer Review Program, expand the availability of administration by the National Peer Review Committee to firms with no AICPA members, and other minor conforming changes, effective for reviews commencing after the implementation of PRIMA, the PRISM replacement system.

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- *Reviewer Alert*:
  - The October issue of this publication offers articles on upcoming peer review changes that become effective in January 2017; a new course on a firm's system of quality control; an update on audits subject to Government Auditing Standards and Single Audit; regulatory developments related to certain offerings exempt from SEC registration; a new report on the AICPA Enhancing Audit Quality initiative; and Peer Review Conference case solutions.
  - The September issue highlights the release of the revised quality control practice aid, developed as part of the AICPA's Enhancing Audit Quality initiative.
  - The August issue includes articles on SSARS No. 21 considerations during a peer review, examples of matters in peer reviews, frequent violations in ethics investigations and how the most recent trends are similar to trends observed in peer review, and links to quality resources to assist firms with improving audit quality.
  - The July issue highlights a Q&A designed to assist reviewers with their understanding of SQCS No. 8 and how those standards should be considered during a system peer review. ■

# Kristy Illuzzi Named New TIC Staff Liaison; Linda Volkert Retires

Linda Volkert, CPA, retired as the AICPA staff liaison for TIC in October 2016. For the past 16 years Linda has served as the heart, soul and key to the success of the Technical Issues Committee. She has a thorough knowledge of standards and standards setting, which has been essential to making the committee's voice more effective and has strengthened our ability to represent the best interests of smaller firms and their private company clients. Her calm approach with a dash of humor has also helped the group stay on point while infusing levity, allowing the group to keep on task and in good spirits while addressing complex topics. We thank Linda for her service and wish her the best in the future.

The Technical Issues Committee is pleased to announce that Kristy Illuzzi, CPA, CGMA, has been named the new AICPA staff liaison for TIC. Kristy is a senior technical manager with the AICPA, where she works with the Center for Plain English Accounting, so she brings with her extensive knowledge about audit and accounting standards, as well as excellent technical writing and research skills. She has been with the AICPA for almost 10 years and started her career in the Audit Practice of Arthur Andersen in NYC. ■

**Let Us Hear From You**

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

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