

Private Company Financial Reporting Committee

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JUDITH H. O'DELL
Chair

Meeting Highlights May 10-11, 2012

Norwalk, Connecticut

In Attendance:

Private Company Financial Reporting Committee (“PCFRC” or “Committee”): Judy O’Dell (chair), Steve Bodine, Steve Shelton, John Burzenski, Tom Groskopf, Mary Ann Lawrence, James Stevenson, Jim Smith, David Lomax and George Beckwith
Financial Accounting Standards Board (“FASB”) member Tom Linsmeier .

FASB assistant director Jeff Mechanick

American Institute of Certified Public Accountants (“AICPA”) staff members, Dan Noll and Bob Durak

Other FASB staff members participated in parts of the meeting as needed for project updates and discussions.

Note that all discussions of FASB projects reflect the project’s status as of the date of this meeting. Check the FASB website for further updates.

The PCFRC met jointly with the SBAC (and the full FASB Board and Technical Director) during its morning session.

Joint Meeting with Small Business Advisory Committee (“SBAC”)

Updates about FAF, FASB, PCFRC and PCAOB Activities

Terri Polley, President and CEO of FAF, spoke about the FAF’s proposal to establish a Private Company Standards Improvement Council. The FAF is considering changes to its original proposal based on stakeholder input and is expected to finalize its plans at its May 23 meeting. Leslie Seidman, chair of the FASB, highlighted a few of the FASB’s projects and provided an overview of some of the recent efforts of the FASB to increase its outreach activities and Gregory Fletcher of the PCAOB informed the committees about recent PCAOB projects and activities. Judy O’Dell, chair of the PCFRC, informed the SBAC about recent activities of the Committee.

Leases

FASB staff spoke to the two committees about the Leases project and explained the issues that the FASB and IASB are currently focusing on. Participants discussed the pros and cons of the four approaches to measuring the cost of a lease over the lease term that the Boards are currently considering. The PCFRC met separately with FASB staff afterwards about other aspects of the Leases project.

Private Company Decision Making Framework

FASB staff updated the two committees about the project to develop a framework for use by the FASB in making decisions about whether and when to allow exceptions or modifications to GAAP for private companies. FASB staff has drafted modules outlining private company user needs and cost/benefit issues relating to recognition, measurement, disclosure, presentation, effective dates, and transition. The Framework is expected to be exposed for public comment this summer.

Each draft module of the Framework was reviewed. Participants' comments were as follows.

- Many participants were supportive of the modules that were presented and were interested in understanding how it would be used and institutionalized in the standard-setting process.
- Some participants suggested that the FASB staff reconsider the proposed requirement for a private company to make an irrevocable decision to avail itself of all of the recognition and measurement private company differences in GAAP or none of them.
- Related to the transition module, some participants stressed the need for comparability between companies' financial statements. Those participants indicated a preference for requiring all private companies to follow the same transition method and not allowing the private companies to early-adopt a standard. Other participants believed that there are situations in which it is more cost-effective for private companies to early-adopt a standard.
- Concerns were expressed about ensuring that the Framework, once finished, is given an appropriately permanent and significant place in the standard-setting process.

The PCFRC continued its discussion of the Framework with FASB staff in its separate meeting.

Definition of a Nonpublic Entity

FASB staff discussed the project to define a nonpublic entity and sought feedback from the two committees. Some participants suggested that the FASB take a more flexible approach to the definition rather than a pass/fail method. Under the suggested approach, there would be a base definition of a nonpublic entity and different gradients of companies as one moved towards being an SEC registrant depending on the nature of the exception/difference. Some Committee members advised that the definition should not be based on a Securities and Exchange Commission definition of a public entity, but rather should be based on access to securities markets and the obligation to provide financial statements.

The PCFRC continued the discussion of this project with FASB staff in its separate meeting.

PCFRC Meeting

Variable Interest Entity Guidance

To aid the FASB staff in their effort to develop improved guidance on the accounting for variable interest entities for private companies, the PCFRC provided the FASB staff with information about the reasons (e.g., tax planning, estate planning, limiting legal liability) why private companies establish separate entities to hold assets, such as office buildings, real estate, and equipment. PCFRC members explained the inter-relationship among a private operating company, its related entities and its owners in typical scenarios. PCFRC members indicated a need for implementation guidance covering common VIE situations encountered at private companies. The guidance should clarify when an entity is a VIE and what entity, if any, should consolidate it.

EITF Issue No. 12-D, “Accounting for Joint and Several Liability for Which the Total Amount of the Obligation is Fixed”

PCFRC members discussed the proposed EITF with the FASB staff. PCFRC members indicated that these obligations are common, especially at healthcare entities and nonprofits. The pros and cons of recording the total amount of the obligation subject to joint and several liability versus recording less than the total amount of the obligation subject to joint and several liability (such as the amount the entity expects to pay or the amount it was allocated) were discussed.

Nonpublic Entity Fair Value Measurement Disclosures

FASB staff sought input from the PCFRC about whether the FASB should engage in a project to evaluate whether there is a basis to exempt nonpublic entities from providing some disclosures about fair value measurements determined under the Level 3 fair value hierarchy. PCFRC members discussed the potential cost savings and benefits of such a project and focused particularly on whether a narrative disclosure of the reasons for significant changes in the amount of assets and liabilities measured under Level 3 of the fair value hierarchy would be a cost-effective alternative to the existing requirement to disclose tabular reconciliations from the opening balances to the closing balances. Generally, PCFRC members did not believe that the project would yield significant cost savings for private companies and perhaps the FASB’s time would be better spent on other projects (e.g., possibly removing tabular reconciliation requirements for warranty obligations.)

Definition of a Nonpublic Entity

The PCFRC continued its earlier discussion about the project to define a nonpublic entity. The issue of whether or not to include private financial institutions in the definition was considered. Related to that, some PCFRC members believed that such institutions could be included in the definition under a gradient approach in which different types of private entities would be eligible for GAAP modifications depending upon the level of public

accountability and regulation the entity was subject to. PCFRC members believed such an approach would be preferable to a binary (public or nonpublic) approach.

Private Company Accounting Decision Making Framework

Continuing its earlier discussion, the Committee considered the manner in which nonpublic entities would be allowed financial reporting differences in recognition and measurement. Committee members discussed some possible differences in recognition and measurement that would benefit private companies such as differences in the accounting for uncertainty in income taxes, variable interest entities, interest rate swaps, goodwill, and guarantees. Some PCFRC members were not in favor of an approach in which a nonpublic entity would have to make an election to either adopt all potential GAAP modifications concerning recognition and measurement or none of them.

Leases

The PCFRC continued its discussion about the Leases project and provided input to FASB staff about the four approaches to accounting for a lease currently being considered by the FASB. PCFRC members were generally of the opinion that there are two kinds of leases – financing and other than financing – and that the accounting should reflect those differences. Committee members suggested that utilizing a zero-discount option may be a practical expedient when accounting for other-than-finance type leases. In addition, PCFRC members stressed that if the definition of a lease required a specifically identifiable asset, companies could avoid lease accounting by writing leases that allowed for substitution.

Agenda Prioritization, Emerging Trends and Simplification Projects

PCFRC members were informed about a discussion the SBAC had concerning the FASB's project agenda. PCFRC members suggested that the FASB should consider adding projects for the following items to their agenda:

- Other comprehensive income
- Distinguishing between liabilities and equity
- Push-down/new basis accounting

Joint Meeting between the PCFRC and the FASB

The PCFRC discussed the following projects with the FASB. See the meeting highlights above for a description of the points and concerns expressed by the PCFRC to the full Board related to these projects. Additional points and concerns raised by the PCFRC are presented below.

- Revenue recognition
 - PCFRC members provided input about the pros and cons of requiring retrospective application of the proposed revenue recognition standard.

- Variable interest entities
 - The PCFRC informed the Board about the reasons private companies form separate entities to hold real estate and equipment. Members urged the Board to issue implementation guidance to assist private companies in complying with GAAP requirements regarding consolidation of variable interest entities.

- Leases
- Private company decision making framework
- Definition of a nonpublic entity
- Nonpublic entity fair value measurement disclosures

Next PCFRC Meetings and Administrative Matters

The Committee set the following tentative meeting dates for 2012:

- June 28-29 (Norwalk, CT)
- October 4-5 (Norwalk, CT)