Update on AICPA Blue Ribbon Panel (BRP) on Accounting for Private Firms

Dev Strischek, BRP Member and
senior credit policy officer
SunTrust Banks, Inc.
Atlanta GA
Dev.Strischek@SunTrust.com or 404-230-5242

AICPA BRP Update Disclaimer

- The Following presentation reflects my own opinions, observations, and viewpoints, not necessarily those of the BRP, AICPA, FASB, or others involved in this effort
- I'm a user, not a preparer
- FASB's website at www.fasb.org is the official source of BRP information

Agenda Overview

- Forces affecting private company accounting
- Roles of two parallel groups
  - Blue Ribbon Panel on Private Company Accounting
  - Private Company Financial Reporting Committee (PCFRC)
- Models under BRP consideration
- Governance under BRP consideration
- Accounting convergence activities to date
- Implications
- Closing

Forces Affecting Private Company Accounting

- FASB/IASB Convergence Projects- PCFRC early involvement to make sure private company issues are considered
- FASB emphasis on public entity investor needs
- AICPA recognition of IFRS for SME's as GAAP in July 2009
- Increasing tolerance by users of reports with GAAP exceptions
- SEC Roadmap for IFRS adoption
- Efforts in other countries for separate private company accounting
- Recent Deloitte survey: 51% of respondents believed there should be separate accounting standards for private companies

Events and Trends in Other Countries—what universal standard?

- Canadian Accounting Standards Board published ED "Accounting Standards for Private Enterprises"
- UK Accounting Standards Board proposing three tier system of financial reporting
- Japan- Formed Council on Accounting of Unlisted Companies to determine if separate set of accounting standards for unlisted companies should be put in place
- IFRS for SMEs – being used, debated, and modified in many areas of the world

Current Options for Private Companies Absent any National Effort to Address Private Company Accounting

- Continue to follow US GAAP (especially NPOs as IFRS does not address NPO issues)
- Use US GAAP with exceptions
- Convert to full IFRS
- Adopt IFRS for Small and Medium-Sized Entities
- Use tax or cash basis of accounting

FASB/IASB Joint Projects with Private Company Impact

- Financial Statement Presentation ED due 1Q2011
- Revenue Recognition ED issued 6/28/2010
- Leases ED due 3Q2010
- Financial instruments with characteristics of Equity ED 1Q2011
- Loss Contingencies re exposed 3Q2010
- Financial Instruments ED issued 6/24/2010
- Fair Value ED 6/30/2010
- OCI ED 6/15/2010

Current Status of Deliberations and Implications

- All projects scheduled for completion by 6/11
- Unprecedented level of standard setting
- Challenges preparers' ability to implement
- Decision by 4Q whether gradual implementation or Big Bang!
- Even if all projects completed, GAAP and IFRS will not be fully converged
- Education, training, and certification?
- Government—IRS, SEC?

Even after all this work we still face issues and differences . . .

- Error Correction--GAAP requires restatements more often than IFRS.
- Death of LIFO—will IRS repeal LIFO conformity rule?
- Reversals of impairments
- PP&E valuation--component depreciation
- Development costs
- Fair value debate between regulators and FASB—what market value?
- So how much convergence do we want and need?

Origins of BRP--2009 PCFRC Letter to FAF urging consideration of private company accounting issues

Factors influencing PCFRC thinking:

- Difficulty in getting FASB to provide differential standards- FIN 48 and FIN 46R-for private firms
- Recognition that private company users have different needs than investors
- Increasing complexity of standards
- Issuance of SME document and efforts in other countries to address private companies

What's Different about BRP Panel?

- Committee is made up of users (lenders, business owners, private equity, venture capitalist, surety), preparers and practicing CPAs
- Strategic purpose to determine what the future standard setting process should be
- Decision to be made by YE 2010
- Committee sponsored by FAF, AICPA, NASBA

Blue Ribbon Panel Mission

Address how accounting standards can best meet the needs of **users** of U.S. private company financial statements.

Objectives of BRP

(1) Understand the current standard-setting structure and process;

(2) Understand the needs of users of private company financial statements;

(3) Understand the cost benefit considerations of GAAP financial statements for preparers;

(4) Identify alternative structures and standard-setting processes;

(5) Determine if the current process should be modified for the private companies;

(6) Provide recommendations to the FAF Trustees

Blue-Ribbon Panel's April 12, 2010 Meeting

- Understanding the needs of users of private company financial statements
- Users of private company financial statements primarily include lenders, other creditors, bonding and credit agencies, and business owners
- Users like the "gold stamp" of GAAP but would be open to a different "GAAP"
- Users like GAAP for consistency, comparability and assurance
- Most Users adjust the financials to meet their end needs
- Companies, more recently, seem to be taking more exceptions to GAAP

Blue-Ribbon Panel's May 14, 2010 Meeting

- Decided after listening to all users and preparers that they wanted FASB to give their recommendations to possible proposals for private company reporting.
- FASB has a staff member dedicated to this along with asking the chair of the PCFRC for help.

Blue Ribbon Panel's July 19 Meeting

- BRP selected 3 of 7 models for further study
- BRP reviewed 6 governance structures
- BRP asked FASB to solicit public comment on the model alternatives through its website and present the results at the next BRP meeting in October
  - If you're interested in commenting, go to www.fasb.org home page

Seven Models at 7/19 BRP Meeting

- US GAAP-Based "Homegrown" Models
  - Model 1-US GAAP w/ exclusions for private companies-current system
  - Model 2-US GAAP w/exclusions for private companies-with enhancements
  - Model 3-US GAAP-Baseline GAAP w/public company add-ons
  - Model 4-Separate, stand-alone GAAP based on current US GAAP
  - Model 5-Separte, stand-alone GAAP from ground up based on new framework
- IFRS-Based Models
  - Model 6-Unmodified IFRS for SME's
  - Model 7-IFRS for SME's customized for US private companies

BRP picked Three Models . . .

- US GAAP-Based "Homegrown" Models
  - Model 1-US GAAP w/ exclusions for private companies-current system
  - **Model 2-US GAAP w/exclusions for private companies-with enhancements**
  - **Model 3-US GAAP-Baseline GAAP w/public company add-ons**
  - **Model 4-Separate, stand-alone GAAP based on current US GAAP**
  - Model 5-Separte, stand-alone GAAP from ground up based on new framework
- IFRS-Based Models
  - Model 6-Unmodified IFRS for SME's
  - Model 7-IFRS for SME's customized for US private companies

7/19 BRP Governance Options

- Structures for US GAAP-based Homegrown Models
  - Structure A-Current FASB Board
  - Structure B-Restructured FASB Board w/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 SME's in addition to IASB Board
    - Current FASB Board
    - Restructured FASB Board
    - New, separate Private Company Standards Board

BRP Preferences at 7/19 Meeting

- Structures for US GAAP-based Homegrown Models
  - Structure A-Current FASB Board
  - **Structure B-Restructured FASB Board w/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 SME's in addition to IASB Board
    - Current FASB Board
    - **Restructured FASB Board**
    - **New, separate Private Company Standards Board**

Meanwhile, AICPA approved SME last year . . .

- Published July 13, 2009 on www.ifrs.com
- No barriers to use in US- but users need to be consulted
- IFRS is now an acceptable form of GAAP- not an OCBOA
- Guidance in audit, review and comp literature on how to report
- Not all state licensing authorities accept it—Ohio does not
- Some private companies may find IFRS for SMEs attractive alternative to US GAAP
- Increased comparability if looking to do business overseas

SME- Pros and Cons

- Pro- will not change for 2 years- so no need to keep up to date on IFRS changes
- Pro- self contained and easy to read
- Con- more principles based- more need for judgment
- Con- IFRS expects preparers to explain details in much lengthier footnotes
- Con- implementation may be difficult
- Con- set by IASB- less chance for US users to influence changes

SME Modification of IFRS

- Topics omitted
- Only simpler options included
- Recognition and measurement simplifications
- Disclosure reductions
- Redrafting in "plain English"- which also makes it easier to translate- and easier for users to understand

Only Simpler Options Included

- Cost depreciation for investment property
- Cost-amortization-impairment model for PP&E and intangibles
- Expense borrowing costs
- Indirect method for cash flows
- One method for all grants
- Expense development costs

Key Differences – IFRS for SMEs and US GAAP

- Disclosures simplified- more emphasis on cash flow info and reconciliations
- LIFO prohibited
- Goodwill and indefinite life intangibles amortized over period not exceeding 10 years
- Depreciation based on components approach
- Reversal of impairment charges allowed

Implementing IFRS for SME

- Applicable to first financial statements that conform to SME
- Must make explicit and unreserved statement that financial statements in compliance with SME
- SME requires 2 year comparative
- Adjustments to opening retained earnings
- Disclose changes in a reconciliation

Summary and Closing

- Forces affecting private company accounting
- Roles of two parallel groups
  - Blue Ribbon Panel on Private Company Accounting
  - Private Company Financial Reporting Committee (PCFRC)
- Models under BRP consideration
- Governance under BRP consideration
- Accounting convergence activities to date
- Implications—at the end of the day, BRP recommends but FASB makes the final call for now . . .

Questions?

- **www.pcfr.org**
- **www.fasb.org for info on BRP**
- Dev.Strischek@SunTrust.com or 404-230-5242