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Susan M. Cospers, CPA
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Re: June 26, 2013 Exposure Draft of a Proposed Accounting Standards Update (ASU), *Presentation of Financial Statements (Topic 205): Disclosure of Uncertainties about an Entity's Going Concern Presumption* [File Reference No. 2013-300]

Dear Ms. Cospers:

One of the objectives that the Council of the American Institute of Certified Public Accountants (AICPA) established for the PCPS Executive Committee is to represent the views of local and regional firms on professional issues in keeping with the public interest, primarily through the Technical Issues Committee (TIC). This communication is in accordance with that objective. These comments, however, do not necessarily reflect the positions of the AICPA.

TIC appreciated the opportunity to discuss its comments on this ED with the Board and staff at the FASB/TIC Liaison Meeting on September 27, 2013. TIC has re-examined the ED and is providing the following comments for your consideration.

TIC has not responded to Questions 3 (part 2), 6, 7, 11(e), 16, 17 and 19, which pertain to SEC registrants only. TIC's responses to the questions for respondents below are solely in the context of nonpublic entities.

GENERAL COMMENTS

TIC appreciates the Board's efforts to date in developing this proposal. Going concern disclosure is a sensitive and emotional topic, especially for business owners, and it requires careful consideration and extensive deliberation. Although TIC disagrees with certain aspects of the proposal, TIC members have always been very supportive of having a standard within U.S. GAAP for the disclosure of going concern uncertainties.

TIC supports the definition of the going concern presumption, the requirement for a management assertion and disclosure regarding going concern uncertainties and the exemption from the "substantial doubt" determination for non-SEC filers.

TIC disagrees with the need for a formal, rolling 24-month interim assessment of going concern and the length of the assessment period. TIC is recommending a trigger-based disclosure threshold for interim periods and a shorter assessment period for nonpublic entities.

TIC was unable to reach a consensus on the appropriate disclosure threshold for going concern uncertainties. However, all TIC members agree that if the Board moves forward with the proposed disclosure threshold, the Board should clarify the distinction between the probable and “more likely than not” (MLTN) assessment thresholds, eliminate or clarify the distinction between inside v. outside the ordinary course of business, provide more guidance on the extent of disclosure required (especially for the MLTN threshold) and provide an additional transition year for nonpublic entities.

Further details on TIC’s recommendations are discussed below.

SPECIFIC COMMENTS

Question 1: *The proposed amendments would define going concern presumption as the inherent presumption in preparing financial statements under U.S. GAAP that an entity will continue to operate such that it will be able to realize its assets and meet its obligations in the ordinary course of business. Do you agree with this definition? If not, what definition should be used and why?*

TIC agrees with the definition.

Question 2: *Currently, auditors are responsible under the auditing standards for assessing going concern uncertainties and for assessing the adequacy of related disclosures. However, there is no guidance in U.S. GAAP for preparers as it relates to management’s responsibilities. Should management be responsible for assessing and providing footnote disclosures about going concern uncertainties? If so, do you agree that guidance should be provided in U.S. GAAP about the timing, nature, and extent of footnote disclosures about going concern uncertainties for SEC registrants and other entities? Why or why not?*

Yes, management should be responsible for assessing and disclosing going concern uncertainties and for assessing the adequacy of related disclosures. The auditor’s responsibility should be to audit this assessment and disclosure.

Currently, management makes various assertions/representations regarding the realizability of individual assets during the course of an audit (e.g., a deferred tax asset is realizable or not; a long-lived asset is impaired or not; a loan is collectible or not; etc.). However, the authoritative accounting standards have not previously required management to make an assertion regarding the ultimate realizability of the net assets / viability of the entity. That assessment has always been part of the auditor’s responsibility. The model for assessing going concern today reverses the traditional roles of management and auditor and is therefore inconsistent with other accounting standards. The proposed ASU would correct this misalignment. TIC therefore agrees that

the assessment and disclosure requirements for going concern uncertainties belong in the accounting standards.

Additionally, TIC believes it is important to note that many nonpublic entity financial statements are not audited; rather, they are either compiled or reviewed or prepared by management without the assistance of an external accountant. Therefore, what may or may not be in the auditing standards is irrelevant to what the accounting standards should include. Accounting standards, particularly disclosures as sensitive and important to users as going concern, should not be influenced by the level of attest service associated with the financial statements.

Question 3 (in part): *Would the proposed amendments reduce diversity in the timing, nature, and extent of footnote disclosures and provide relevant information to financial statement users?*

The proposed amendments would likely result in more consistency than currently exists, but given the nature of professional judgment and various perspectives of preparers (e.g., some entities are more aggressive than others in reporting); there will still be some diversity in practice.

Question 4: *The proposed amendments would require management to evaluate going concern uncertainties and additionally, for SEC filers, to evaluate whether there is substantial doubt about the entity's ability to continue as a going concern. An alternative view is that such evaluations should not be required because management would inherently be biased and, thus, the resulting disclosures would provide little incremental benefit to investors. Do you believe that an entity's management has the objectivity to assess and provide disclosures of uncertainties about the entity's ability to continue as a going concern? Why or why not? If not, please also explain how this assessment differs from other assessments that management is required to make in the preparation of an entity's financial statements.*

Yes, most TIC members agree that management personnel can and should assess and provide disclosures regarding going concern uncertainties. While that assessment may not always be without management bias, that risk will be a consideration in any audit, review or compilation engagement whenever subjective judgments and estimates come into play.

The Clarified Auditing Standards (*AICPA Professional Standards*, AU-C Section 540, *Auditing Accounting Estimates*, paragraph 21) already require auditors to review the judgments made by management for indicators of possible management bias. For any engagement, however, TIC believes the risk of management bias is not reason enough to reject the notion that management has a responsibility to assess going concern uncertainties.

Ultimately, the financial statements are management's responsibility. If going concern requirements are to be transferred to the authoritative accounting standards, which TIC

supports, preparers must take responsibility for the assessment and disclosure of going concern, as they would for any other aspect of the financial statements. TIC believes the proposal mitigates the risk of management bias for non-SEC filers in that management will not be required to use “substantial doubt” language in the disclosure thus avoiding the stigma of a self-fulfilling prophecy that is often attached to those words. This takes some of the emotion out of the going concern disclosure and may help management prepare objective disclosures.

Question 5: *At each reporting period, including interim periods, the proposed amendments would require management to evaluate an entity’s going concern uncertainties. Do you agree with the proposed frequency of the assessment? If not, how often should the assessment be performed?*

TIC believes the proactive assessment proposed in the ED, which would require management to evaluate the likelihood that the entity would be unable to meet its obligations as they become due within 24 months of the balance sheet date, should be performed annually for nonpublic entities, not at each interim period. Performing a rolling 24-month assessment, whereby management would have to forecast potential going concern uncertainties that would occur in the interim period(s) following the annual period, would be unnecessary and time-consuming for nonpublic entities.

Management should be required to perform an interim assessment and additional disclosure only if:

- certain trigger events occur during the interim period or circumstances exist as of date that the interim financial statements are available to be issued, that did not exist at the time of the issuance of the annual financial statements that would indicate the need to reassess going concern disclosures or the going concern basis of accounting; or
- information comes to management’s attention during the interim periods that prior assumptions and considerations about going concern uncertainties were determined to be inaccurate.

TIC believes management would have a responsibility to be knowledgeable about the occurrence of any triggering events.

This change would simplify the standard without compromising the public interest and would promote the timely issuance of the interim financial statements.

Questions 6 and 7 are omitted.

Question 8: *The proposed footnote disclosures about going concern uncertainties would result in disclosure of some forward-looking information in the footnotes. What challenges or consequences, if any, including changes in legal liability for management and its auditors, do you anticipate entities may encounter in complying with the proposed disclosure*

guidance? Do you foresee any limitations on the type of information that preparers would disclose in the footnotes about going concern uncertainties? Would a higher threshold for disclosures address those concerns?

TIC believes that preparers will raise valid concerns regarding the disclosure of specific conditions or events that have not yet occurred and are only MLTN to occur in the future and that could put the entity at a competitive disadvantage. For example:

- a. Customers and vendors may be able to negotiate sales/purchase terms to their benefit.
- b. Competitors may learn trade secrets or confidential information (e.g., upcoming expiration of a key patent, as discussed in paragraph 205-40-50-4[d] of the ED).
- c. Attorneys involved in litigation against the preparer may use the going concern disclosure information to gain an advantage in the litigation.

TIC believes the above concerns are especially challenging for entities to accept given the varying interpretations that exist concerning the concept of MLTN. TIC therefore encourages the Board to provide additional disclosure guidelines if the probable and MLTN thresholds are retained in the final ASU.

To meet the challenges inherent in the proposed disclosure threshold, many nonpublic entities will need time to adjust their mindset and approach to going concern uncertainties. Practitioners, in many cases, will need additional training to guide their clients through the new standard. TIC therefore requests that the Board provide an additional year of transition for nonpublic entities beyond the effective date for public companies.

Question 9: *What challenges, if any, could auditors face if the proposed amendments are adopted?*

TIC believes auditors would encounter the following challenges with the proposal:

- a. Uncertainty as to when it's MLTN that the entity will be unable to meet its obligations in the next 12 months.
- b. Auditing various management representations and assertions regarding:
 - the likelihood that the entity will not be able to meet its obligations within the 24 months after the financial statement date;
 - the likelihood of management's plans being effectively implemented; and
 - the likelihood of management's plans mitigating the adverse conditions and events.
- c. Determining when management's plans are outside the ordinary course of business.
- d. Finding objective audit evidence regarding management's future plans more than one year in the future.

Question 10: *Do the expected benefits of the proposed amendments outweigh the incremental costs of applying them?*

TIC is uncertain whether the benefits of the standard will outweigh the additional implementation costs for nonpublic entities. Additionally, TIC believes the ED is overly complex and that simplifying the standard could reduce costs. To achieve this, TIC believes the following modifications should be made to certain proposed requirements.

- Shorten the assessment period. A shorter assessment period would reduce the time and management expertise needed for the assessment and potentially facilitate the practitioner's audit or review procedures since more objective audit or review evidence may be available to evaluate management's going concern assessment. See Question 12 below for TIC's specific recommendation.
- Eliminate or clarify the disclosure assessment which depends on management's plans being inside v. outside the ordinary course of business. If the assessment is retained, clarify what is acceptable within the context of "inside the ordinary course of business" in the nonpublic entity context. See Questions 13/14 below for further details.
- Eliminate the rolling 24-month going concern assessment for interim periods in favor a trigger-based threshold for nonpublic entities. See Question 5 above for TIC's specific recommendation.

Disclosure Threshold

Question 11: *Under the proposed amendments, disclosures would start at the more-likely-than-not or at the known or probable threshold as described in paragraph 205-40-50-3.*

- a. Is the disclosure threshold appropriate? What are the challenges in assessing the likelihood of an entity's potential inability to meet its obligations for purposes of determining whether disclosures are necessary?*
- b. Are there differences between assessing probability in the context of transactions and assessing probability in the context of the overall state of an entity that are meaningful to determining the appropriateness of a probability model for assessing substantial doubt?*
- c. Do the proposed amendments adequately contemplate qualitative considerations? Why or why not?*
- d. Do you believe that the guidance in paragraph 205-40-50-4 about information on how an entity should assess the likelihood of its potential inability to meet its obligations and the implementation guidance within the proposed amendments are helpful and appropriate? Why or why not?*

Assessing the probability of an entity's ability to continue as a going concern is not the same as assessing probability in the context of a particular transaction. Assessing the overall state of an entity is a highly complex determination because a myriad of considerations, including subjective estimates, judgments and interrelationships, need to be evaluated. Such considerations are relevant for each step of the going concern

assessment. In addition, assessing the overall health of an entity is a very emotional exercise for management and is potentially contentious and adversarial in nature.

TIC members were split in their opinions concerning the proposed disclosure threshold and were unable to reach a consensus. Although a slight majority of TIC members supported earlier disclosure in the form of a MLTN threshold, a significant minority favored a single, higher threshold.

TIC believes the distinction between MLTN and probable will be one of the most difficult provisions of the ED to implement for nonpublic entities. The Master Glossary of the FASB *Accounting Standards Codification*TM (ASC) includes two definitions of “probable” but no definition of MLTN. Probable is perceived by some as at least a 70-80% likelihood of occurrence while others have either a lower or higher threshold based on a different interpretation of when a future event is “likely to occur.” The web-based version of the ASC links to the usage of the term in various ASC topics, so that its usage can be interpreted in context. The term MLTN is defined in ASC paragraph 740-10-25-6 in relation to uncertain tax positions as “a likelihood of more than 50%.” However, since MLTN is not defined in the Master Glossary, some may believe that the definition in ASC Topic 740 may apply only to uncertain tax positions and therefore may assess MLTN as a probability level of 50% or less in another context. TIC believes the definition of a specific term can be interpreted differently depending on the context in which it is being evaluated unless adequate guidance is provided.

If confusion exists on the part of management as to the meaning of the probability thresholds, the resulting disclosures will be inconsistent even among entities with similar circumstances. TIC urges the Board to provide as much clarity as possible on its interpretation of MLTN v. probable.

In addition, some of the members who supported the MLTN threshold could not agree on gross v. net disclosure. For example, some believe that disclosure should not be required until it’s MLTN that the entity would be unable to meet its obligations after the effect of all management plans has been considered.

Irrespective of individual members’ views on the appropriate disclosure trigger, all TIC members agreed that the criteria for differentiating actions that are inside v. outside the ordinary course of business are insufficient, despite the guidance that has already been provided in the ED. TIC also believes that the criteria fail to take into consideration the unique practices that occur within nonpublic entities. See TIC’s response to Questions 13 and 14 below for TIC’s recommendation.

TIC also believes that preparers will struggle with the extent of disclosure required, especially when only the MLTN threshold has been reached. Specifically, the proposal fails to address whether the note disclosure needs to include management’s assessment of the likelihood that the entity will be unable to meet its obligations in the next 24 months. It simply refers to a change in the extent of disclosure as more information becomes available but is silent about how to characterize the uncertainty and the likely

success of management's plans. It's unclear whether the disclosures are meant to be only factual in nature, which would allow users to draw their own conclusions, or whether management is expected to state whether the likelihood of not being able to meet the entity's obligations is MLTN v. probable.

Although the ED does not include a requirement to disclose management's assessment of these probabilities, TIC believes some may conclude that such disclosure was intended by the Board because the two probabilities were considered in determining the need for disclosure. TIC recommends that the final standard include guidance to clarify that management is not required to disclose the likelihood that going concern uncertainties will be realized. Without such guidance, diversity in practice could result, which would be potentially confusing for financial statement users.

Questions 12: *The proposed amendments would require an entity to assess its potential inability to meet its obligations as they become due for a period of 24 months after the financial statement date. Is this consideration period appropriate? Is it appropriate to distinguish the first 12 months from the second 12 months as proposed in the amendments? Why or why not?*

In its consideration of this proposed requirement, TIC tried to balance two competing objectives. First, TIC believes the new standard should discourage the current practice of holding the financial statements open for one year and a day from the balance sheet date to avoid "substantial doubt" disclosures. At the same time, however, the standard needs to establish a reasonable going concern consideration period that is not too forward-looking.

The majority of TIC members therefore recommend requiring an assessment period of twelve months from the date the financial statements are available to be issued. Under TIC's proposal, most nonpublic entities would have an assessment period of 15 to 18 months from the financial statement date, instead of the proposed 24 months. TIC believes this approach is a reasonable compromise, which has already been adopted successfully by one TIC member firm.

Questions 13 and 14:

13. *Under the proposed amendments, management would be required to distinguish between the mitigating effect of management's plans in and outside the ordinary course of business when evaluating the need for disclosures. Is this distinction relevant to determining if and when disclosures should be made? If so, explain how management's plans should be considered when defining the two different disclosure thresholds.*

14: *Do you agree with the definition of management's plans that are outside the ordinary course of business as outlined in paragraph 205-40-50-5 and the related implementation guidance?*

Those TIC members who support a MLTN threshold are almost evenly split on the issue of how to consider management plans. Some favored considering all management plans

(a net assessment) before disclosure would be triggered. Others favored the disclosure threshold in the ED, which would require disclosure if it is MLTN that the entity will be unable to meet its obligations within the assessment period without taking actions outside the ordinary course of business. Accordingly, TIC believes additional outreach to preparers and users in TIC's constituency is necessary to determine the most relevant disclosure threshold.

As noted above, however, all TIC members believe that preparers and practitioners in the nonpublic arena will have difficulty classifying management's plans as inside v. outside the ordinary course of business. Part of the problem is that the guidance in the proposal does not take into consideration the unique operating characteristics of nonpublic entities.

For example, many smaller companies pay for certain personal expenses of the owners and record this as an asset. When the company needs cash to fund payroll or other business expenses, the owner writes a check to the company from personal funds and the company reduces the asset balance. From the owner's perspective, these transfers would be classified as transactions in the ordinary course of business. However, paragraph BC32 implies that they would be considered outside the ordinary course of business because the owner's financing transaction is for the purpose of restoring the company's cash position to maintain ongoing operations.

TIC also believes that most nonpublic entities would consider refinancing to be part of the ordinary course of business and would use the term "restructuring" to refer to action plans designed to renegotiate debt to accommodate financial hardship.

Some TIC members recommend eliminating inside v. outside the ordinary course of business as a factor in the going concern assessment. Those members who hold this view believe eliminating this factor would reduce complexity, mitigate preparer's concerns with the stigma of potentially premature disclosure but still provide earlier disclosure of going concern uncertainties compared to current practice.

As previously stated, if the Board decides to retain the distinction between inside and outside the ordinary course of business, TIC recommends further refinement of the criteria to recognize the operational differences of nonpublic entities.

Question 15: *Do you agree with the nature and extent of disclosures outlined in paragraph 205-40-50-7? Should other disclosure principles be included?*

TIC generally agrees with the nature and extent of the proposed disclosures but is uncertain how the "extent of disclosure" principle would be applied to the initial disclosure of going concern uncertainties that meet the MLTN (but not the "known or probable") threshold, as discussed under Question 11 above.

Questions 16 and 17 are omitted.

Substantial Doubt Determination

Question 18: *Do you agree with the Board's decision not to require an entity that is not an SEC filer to evaluate or disclose when there is substantial doubt about its going concern presumption? If not, explain how users of non-SEC filers' financial statements would benefit from a requirement for management to evaluate and disclose substantial doubt.*

Yes. TIC believes the term "substantial doubt" is an ambiguous term that is applied inconsistently in practice. It also is associated with the stigma of impending bankruptcy resulting in disclosure that management perceives as a self-fulfilling prophecy. The term is unnecessary in the nonpublic arena since the user of nonpublic entity financial statements is often in the best position to assess the going concern status of an entity given the user's access to management. TIC believes removal of the term "substantial doubt" will reduce the risk associated with management bias and promote more transparent disclosure.

Question 19 is omitted.

TIC appreciates the opportunity to present these comments on behalf of PCPS member firms. We would be pleased to discuss our comments with you at your convenience.

Sincerely,



Karen Kerber, Chair
PCPS Technical Issues Committee

cc: PCPS Executive and Technical Issues Committees