pwc

November 11, 2020

Ms. Hillary Salo
Technical Director
Financial Accounting Standards Board
401 Merritt 7, PO Box 5116
Norwalk, CT 06856-5116

RE: File Reference No. 2020-500

Dear Ms. Salo:

PricewaterhouseCoopers LLP appreciates the opportunity to comment on the Proposed Statement of Financial Accounting Concepts, *Concepts Statement 8 - Conceptual Framework for Financial Reporting - Chapter 4: Elements of Financial Statements*. We support the FASB's efforts to periodically revise the Conceptual Framework without reconsidering all aspects of the Framework, or when decisions at the standards level significantly advance the thinking on framework-level concepts. However, as discussed in the Appendix to this letter, we have concerns with the proposal, including the following.

- Definitional changes may result in changes in practice. While we understand that the primary purpose of the Framework is to assist the Board in standard setting, preparers also look to the Framework to develop an appropriate accounting policy in the absence of other guidance.
- Wording changes, such as moving the concept of "control" from the definition of an asset to the guidance that supports the definition, require clarification, in order to ensure that future Boards and other interested stakeholders interpret the concepts consistently with the current Board's intent.
- In some cases, we do not believe the Board's attempts to provide clarity add to the user's understanding. For example, we do not believe that the proposed changes to the definition of an asset reduce complexity around the identification of intangible assets.
- Because of their interdependencies, we believe the presentation chapter, which was deliberated separately, should be redeliberated in order to confirm its continued consistency with the concepts in revised Chapter 4 as proposed.
- The proposal was not unanimously approved by the Board. An argument can be made that changes to the Framework itself should require unanimous approval by the Board given that the primary purpose of the Framework is to assist the Board and future Boards in standard setting.

We are also concerned that the proposed changes could result in incremental costs that, in our view, are not justified by the perceived benefits. Given these concerns, we do not believe that the Board should move forward with the proposed changes at this time.

If you have any questions regarding our comments, please contact David Schmid (david.schmid@pwc.com) at (973) 997-0768 or Maria Constantinou (maria.constantinou@pwc.com) at (908) 447-5556.

Sincerely,

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP

Appendix

Question 1 -The Board expects that most assets that met the definition of an asset in FASB Concepts Statement No. 6, Elements of Financial Statements, will continue to qualify as assets under the definition of an asset in this proposed chapter. Do you agree that the definition of an asset in this proposed chapter is consistent with the Board's assertion? If not, please provide examples.

We believe there will be many questions as to how to apply the proposed definition and whether it might be interpreted differently by future Boards. Some of the proposed language suggests that what meets the definition of an asset could change under the revised definition. For example, the gating question of whether something embodies a "probable" future benefit has been removed from the definition in the proposed chapter. We believe this may result in more items meeting the definition of an asset. It is not clear whether this was intentional and the Board instead intends for probability to be considered as part of measurement, in which case an item meeting the definition of an asset might be recorded but have little to no value ascribed to it based on a low likelihood of that benefit materializing. If this is the Board's intent, it would be helpful if that could be clearly stated.

Question 2 - In particular, respondents are asked to focus on internally generated intangible assets. Is the definition of an asset in this proposed chapter helpful in resolving issues of identifying intangible assets?

We do not believe that the proposed definition of an asset resolves issues associated with identifying intangible assets using the definition in the Conceptual Framework. It is our experience that the complexity with intangible assets is not whether they meet the definition of an asset, but instead when to recognize and how to measure them. We do not believe that the proposed revisions to the Framework will reduce complexity in accounting for intangible assets.

Further, paragraph E35 states "Some activities are undertaken with the expectation of obtaining an economic benefit in the future. Examples include research and development, advertising, training, start-up activities, and pre-operating activities. While the costs incurred in these activities are not assets, the activities may result in an entity obtaining an asset or enhancing an existing asset. For these and similar activities, assessments of when a present right exists and whether the right is to a related economic benefit may be especially uncertain..." This seems to imply that expenditures incurred in anticipation of future benefit may not be considered assets, but that the related benefits may meet the definition of an asset. It would be helpful for the Board to clarify how that determination should be made. We are concerned that this determination may not be operable.

Question 3 - The Board's definition of an asset in this proposed chapter does not include the term control. However, this proposed chapter explains why and how control is interrelated to the definition of an asset. Is this discussion sufficient or is the term control necessary to include in the definition of an asset? If the term control is necessary to include, please explain how its inclusion would change the population of items that would meet the definition of an asset in this proposed chapter.

We are not clear why the term "control" has been excluded from the proposed definition of an asset and instead included in the paragraph following the definition. We believe that it would be helpful for the Board to clarify if they intend for this amendment to result in a different outcome compared to the existing definition. If the Board does not intend for this change to result in a different outcome, we are unclear on the reason for the change.

Further, we agree with Ms. Botosan's dissent on this point. It is noted that Ms. Botosan... "believes that control is sufficiently important that it should be elevated from the explanatory paragraphs to the definition itself. She believes that explicit inclusion of control in the definition helps establish the link between an economic resource and a particular entity, which is necessary for an item to be considered an asset of the entity. Ms. Botosan believes that including control in the definition would mitigate potential misapplication of the definition to economic resources to which an entity has a right but no ability to control."

An argument can be made that changes to the Framework itself should require unanimous approval by the Board given that the primary purpose of the Framework is to assist the Board and future Boards in standard setting.

Question 4 - The Board decided that an obligation to transfer either assets or, in certain limited circumstances, an entity's own shares would meet the definition of a liability. Is the discussion in this proposed chapter of the limited circumstances in which the entity's own shares would meet the definition of a liability sufficiently clear?

No. It is not clear whether the ability to transfer either fixed or variable shares would qualify an obligation as a liability. As stated in paragraph E38, the ability to "transfer or otherwise provide economic benefits to others" is required for an obligation to meet the definition of a liability. Paragraph E58 also states that the "transfer of shares sufficient in number to satisfy an obligation of determinable or defined amount is a transfer of an economic benefit. If arrangements permit or require settlement of obligations by issuance of a variable number of the entity's own shares, those shares are essentially being used in lieu of assets to settle an obligation and therefore meet the definition of a liability."

This suggests that an obligation that can be settled by issuing a variable number of shares for a fixed dollar amount would meet the definition of a liability. However, under this definition, any instrument that transfers equity (e.g., a warrant) could also transfer economic benefit and, thus, be considered a liability. It would be helpful if the Board could clarify whether this is their intent.

Question 5 - Other than as described in Question 4, to allow certain share-settled instruments to be liabilities, the Board expects the liabilities that met the definition of a liability in Concepts Statement 6 will continue to qualify as liabilities under the definition of a liability in this proposed chapter. Do you agree that the definition of a liability in this proposed chapter is consistent with the Board's assertion? If not, please provide examples.

It is not clear whether most liabilities that currently meet the definition of a liability will continue to qualify as liabilities under the amended definition. Consistent with our comments in Question 1 regarding the removal of probability from the definition of an asset, removal of probability may result in more items meeting the definition of a liability. Again, we question whether this is the Board's intent or if the Board intends for probability to be considered as part of measurement.

Question 6 - In practice, the more challenging applications of the definition of a liability in Concepts Statement 6 were related to business risks, constructive obligations, and stand-ready obligations. Is the discussion of those three areas in this proposed chapter adequate to understand and apply the definition of a liability?

We believe that the discussion of business risks, constructive obligations, and stand-ready obligations identifies these as areas that are challenging, but does not include clear guidance. For example, one of the more challenging issues associated with these areas relates to determining when an item meets the definition and the "event" that triggers the recording of a liability. The chapter would be more helpful if it provided clearer guidance on these questions.

Question 7 - The Board suggested that integration with presentation principles would be helpful in distinguishing between the components of comprehensive income. To facilitate this distinction, paragraph E92 of this proposed chapter references presentation principles. Is distinguishing revenues from gains and expenses from losses essential as a matter of elements, or should those distinctions be exclusively a matter for presentation concepts? Please explain.

In the absence of specific income statement presentation guidance in the Codification, practice often looks to the definitions of the elements, suggesting that the presentation principles are integrally related to elements. This was recently the case with accounting for government grants as entities receiving CARES Act assistance grappled with whether to present inflows as revenue or other income. This also occurs in other areas of the Codification that lack presentation guidance, such as collaborative arrangements in the scope of ASC 808 or interest income. For this reason, we believe that presentation concepts should be redeliberated concurrent with the proposed amendments.

Further, paragraph E92 states that because a "…primary purpose of distinguishing gains and losses from revenues and expenses is to make displays of financial information about an entity's sources of comprehensive income as useful as possible, fine distinctions between revenue and gains and expenses and losses are principally matters of presentation. Ultimately, those decisions will be made at a standards level …" However, as noted above, many standards do not prescribe presentation, and therefore, the Framework is looked to for guidance. Additionally, this paragraph suggests that a primary purpose of defining revenue is to determine which inflows should be presented as revenue. If the Board does not intend for the definition of revenue (as an example) to be used in determining whether a transaction should be presented as revenue, we think it would be helpful to clearly state that conclusion.

Question 8 - As described in Question 7, this proposed chapter seeks to distinguish between revenues, expenses, gains, and losses. Do the definitions of and other explanatory language related to revenues, expenses, gains, and losses make the distinction between these elements sufficiently clear?

If the intention of this chapter is to provide a principle that establishes the distinction between "revenue" and "gains," we do not believe it is successful. The chapter provides examples of inflows that may be revenue or gains, but removes the underlying principle of "ongoing major or central operations" from that determination. For example, there is well-established practice that certain entities present interest as part of revenue while others present it as part of other income based on whether it is part of their "ongoing major or central operations." We believe that removing "ongoing major or central operations" from the definition of revenue will be difficult to operationalize and might have unintended consequences, such as expanding the scope of inflows that are considered revenue. For example, paragraph E88 states that revenue includes inflows from "other activities" such as interest, rent, royalties, and charitable contributions without applying the filter of whether it is part of "ongoing major or central operations." By removing this, we believe that the proposed definition of revenue lacks a central concept or principle.

There also appears to be internal inconsistency throughout the chapter related to whether entities need to consider what is ongoing major or central to their business in determining whether an inflow is revenue. For example, paragraph E90 states that "Distinctions between revenues and gains and expenses and losses from exchange transactions of an entity depend to a significant extent on the nature of the entity and the activity with which an item is associated. An identical item can be used by entities differently." Paragraph E91 also refers to "routine transactions that result in recognizing revenue." Both of these seem to imply that entities do, in fact, need to consider what is part of their routine or central operations to distinguish revenues and expenses from gains and losses. It is not clear how this ties into the proposed definition which excludes this concept.

We have observed that there is often confusion in practice about whether “other income” is a subset of “gains” or “revenue” and we often see “gains” and “other income” used interchangeably. Adding to the confusion is the fact that the Codification has the broad category “Revenue,” which includes ASC 610 *Other income*, and ASC 610-20 and ASC 610-30 each have subsections that discuss gains. It would be helpful if the Board could clarify in this chapter whether “other income” is different from “gains.”

Finally, we believe that paragraph E89, which lists common circumstances resulting in gains and/or losses, may cause confusion and should be clarified. Certain items on the list are also commonly considered revenue (e.g., nonreciprocal transactions, which can be revenue for not for profit entities, and exchange transactions). For example, ASC 958-605-25-1 states that "Exchange transactions shall be accounted for in accordance with other applicable Topics, such as Topic 606 on revenue from contracts with customers.” We believe explanation of the concept would be more helpful than a list of examples.

Question 9 - The Board has concluded that, other than when exceptions are specifically noted in this proposed chapter, the elements described in this proposed chapter would apply to not-for-profit organizations. Do you agree with this conclusion?

Yes, we agree that the elements described in this chapter would generally apply to not-for-profits (NFPs). However, the Framework only defines elements as revenues, expenses, gains, and losses. We question whether there is a fifth element, equity transfers, for NFPs because they are, by definition, not revenue, expenses, gains, nor losses. Equity transfers are also not investments by or distributions to owners since NFPs do not have owners.

Question 10 - This proposed chapter was developed on the basis of Concepts Statement 6, though several paragraphs have been removed or adapted. Are any of the paragraphs from Concepts Statement 6 that have been removed in drafting this proposed chapter necessary to keep? If so, why?

We have no specific recommendations related to this question.

Question 11 - “Appendix A: Accrual Accounting and Related Concepts,” includes discussion of several concepts that are used in this proposed chapter and in other chapters of the Conceptual Framework. Is this material helpful in a chapter discussing the elements of financial statements?

No. We believe that Appendix A should be removed from the elements chapter since it relates to recognition concepts.