MINUTES OF THE APRIL 1 & 2, 2019 PRIVATE COMPANY COUNCIL MEETING

Location:	FASB Offices 401 Merritt 7 Norwalk, Connecticut
Meeting Date:	Monday, April 1, 2019 Tuesday, April 2, 2019
Starting Times:	April 1, 2019, 3:50 p.m./April 2, 2019, 8:35 a.m.
Concluding Times:	April 1, 2019, 5:30 p.m./April 2, 2019, 12:40 p.m.

PCC Members Present:
Candace Wright (Chair)
Timothy Curt
Jeremy Dillard
David Hirsch
David Lomax
Michael Minnis
Richard Reisig
Dev Strischek
Frank Tarallo
Beth van Bladel
Yan Zhang

FASB Board Members Present:
Russell Golden (Chairman)
Christine Botosan
Marsha Hunt (FASB – PCC Liaison)
Hal Schroeder
Gary Buesser

FASB Board Members Absent:
James Kroeker (Vice-Chairman)

FASB Staff Present:

Susan Cosper	*Jason Bond	*Celine Olcott
Jeffrey Mechanick	*Lucy Cheng	*Rachel Cole
Richard Cole	*Aarika Friend	*Tyler Padgett
Darien Williams	*Liz Gagnon	*Daniel Verburg
Rebecca Harris	*Jenifer Wyss	*Madeline Nash
*Chris Roberge	*Mary Mazzella	*Sophia Ginotti
*James Starkey	*Danielle Fontaine	

FAF Representatives Present:
*Diane Rubin, FAF Trustee (by telephone)

*For certain issues only.

Introductory Remarks

The PCC chair welcomed PCC members, FASB members, and FASB staff to the Council's April meeting.

Town Hall Update

The PCC discussed four upcoming Town Hall Meetings:

1. In June, certain PCC members, FASB members, and FASB staff will be attending the National Advanced Accounting and Auditing Technical Symposium (NAAATS) conference in Las Vegas.
2. During the week of August 11, the PCC, FASB, and FASB staff will have representatives attend the American Accounting Association (AAA) meeting in San Francisco and, through one of the PCC members, will try to combine that trip with a Silicon Valley/San Francisco meeting with the National Venture Capital Association (NVCA).
3. Following a highly successful PCC Town Hall in 2018, the Risk Management Association (RMA) expressed interest in setting up another Town Hall/roundtable with representatives of the PCC, FASB, and FASB staff to be scheduled for fall 2019.
4. The PCC, FASB, and FASB staff are also considering hosting a PCC Town Hall at the California Society of CPA's Accounting & Auditing Conference on October 24-25.

PCC Issue No. 2018-01, "Practical Expedient to Measure Grant-Date Fair Value of Equity-Classified Share-Based Awards"

The FASB staff provided an overview of the project that the PCC added to its agenda at its December 2018 meeting, to develop a practical expedient for private companies for measuring the current price of the underlying stock in an equity-classified share-based-payment award (SBP). The practical expedient would allow private companies to use the exercise price of the underlying stock as its current price for purposes of determining the grant-date fair value of equity-classified awards as long as the awards are not issued in-the-money.

As a result of feedback obtained during the December 2018 PCC meeting, PCC members requested that the staff refine the language of the proposed expedient in addition to identifying any potential issues and developing solutions for those issues. The staff highlighted that, based on the feedback received from Board members during small group meetings, it was determined that additional outreach was needed to further learn about the processes used by preparers for establishing exercise prices and how practitioners are auditing those processes.

The PCC chair began the discussion by asking Board members what concerns they had based on the initial language in the proposed practical expedient. The primary concern shared by several Board members was that they were not certain whether the difficulties with accounting for the current price of the underlying share of an SBP was an accounting issue or an auditing issue. These Board members asked several questions about this throughout the meeting.

The FASB chair asked several questions to gain a better understanding of what is currently done in practice to determine the exercise price of an SBP. One PCC member commented that various methods are employed by companies to establish the exercise price of an SBP. The level of robustness of the valuation performed generally depends on the sophistication of the private company. Valuations can range from a detailed tax-compliant valuation in accordance with Internal Revenue Code Section 409A (a 409A valuation) to an internal valuation based on multiples of financial measures (revenue, EBITDA, and so forth). The FASB chair asked whether, in the absence of an audit, private companies would still obtain a robust valuation to ascertain the exercise price of an SBP. The reasoning behind the question was to determine whether a significant cost reduction would be realized if the issue were addressed through standard setting (a practical expedient) or, if a practical expedient was provided, whether auditors would still require a robust valuation. The same PCC member also noted that the practical expedient would not change how his firm determines the price of an award. A Board member stated that it was her belief that management behavior would only change if management believed that the practical expedient would produce an estimate that was within a reasonable range for the exercise price in a cost-effective manner.

One PCC member stated his belief that the practical expedient would require management to assume more accountability for their valuation process because current practice is to just do whatever the auditors request. The FASB chair asked how the proposed practical expedient would place a burden on management aside from just requiring a management representation letter. The same PCC member stated several times that the reason financial executives and CFOs do not rebut auditor opinions that the valuation has produced an incorrect exercise price is because the effort would only result in additional audit costs in determining an expense that most stakeholders have expressed provides only marginal value. Another PCC member noted that financial statement users do not place a lot of reliance on the estimate and that it is typically only used as a red flag to signal the price at which the option is being issued. Several PCC members stated that users have noted that they are not as concerned with the precision of the estimate, so the practical expedient would further signal to financial statement users that the underlying calculations are only an estimate. If users do not place a lot of reliance on this estimate, PCC members questioned why auditors are placing undue emphasis on determining a precise amount.

A Board member asked how often auditors disagreed with the fair value of the underlying shares determined by an internal valuation. Several PCC members responded that auditors generally do not require significant changes. In other words, although private companies typically comply with auditor and valuation experts' requests for additional information to substantiate internal valuations, the current price of the underlying share used for determining grant-date fair value is generally unchanged.

In response to a question from the FASB chairman, a PCC member (practitioner) asserted that a tax-compliant 409A valuation typically does not require additional audit work. However, he would prefer not to require practice to obtain a 409A valuation to substantiate the current price of the underlying share. Another PCC member, also a practitioner, expressed his view that auditors may require differing levels of information to get comfortable with the estimates, depending on how robust the internal valuation was.

A Board member noted that the PCC's SBP project has considered various options to reduce costs since 2013, and all previously recommended solutions were rejected for various reasons.

That Board member was concerned that the path of the project is now targeted at eliminating audit costs, not preparer costs, which is not in the FASB's purview. Several PCC members agreed with this assertion. The FASB chair then suggested a joint discussion with the AICPA Auditing Standards Board to better understand the rationale for the significant audit procedures, even when the SBP amounts recognized are not expected to be significant. One PCC member (practitioner) asserted that audit procedures would be reduced if a practical expedient was provided that allowed a presumption that awards are not issued in the money.

The FASB chairman requested additional research to be done to determine how often stock options are issued with puts and calls, to gain a better understanding for the potential pervasiveness of those features. He noted that those features would reduce the population of private companies that would be eligible to elect the expedient, because in many instances, the presence of puts or calls would result in liability-classified awards. That limitation, together with instances of private companies not electing the expedient because of strategies to go public, might call into question whether the population of companies that *would* elect the expedient is large enough to warrant standard setting. Based on these observations, the FASB chairman suggested that consideration be given to broadening the scope of the potential expedient so that it could be expanded to more than just the current price input needed to determine grant-date fair value for share option awards.

The FASB chairman also asked the PCC working group, in conjunction with the FASB staff, to conduct outreach to better understand:

1. The trends in compensation (and what's causing them) and whether those trends are moving towards issuing restricted stock units (RSUs), as they are with public companies
2. Whether puts/calls are annual or longer-term
3. Whether accounting practice has ever relied solely on management representations for estimates in other areas.

The PCC chair then summarized the additional outreach that would be needed for the Board to get comfortable with the proposed practical expedient, which included the following:

a. How the exercise price is set
b. How pervasive stock options are
c. The amount and nature of cost savings.

Implementation Topics—Leases & Revenue Recognition

The FASB staff discussed the Board's implementation activities for Topic 842, Leases, and Topic 606, Revenue from Contracts with Customers. The PCC members and FASB staff engaged in specific dialogue related to each Topic as well as a more general discussion of overall trends in private company implementation activities.

The staff began the discussion of leases by providing an analysis of the areas of the Topic for which technical inquiries have been received. The staff then discussed Accounting Standards Updates (ASUs) related to leases that have been issued since the last implementation update at the October 2018 PCC meeting. A PCC member noted that inquiries related to transition make up the largest percentage of total lease inquiries and, as a result, suggested that the FASB provide additional education to private companies on how to recognize leases on the balance sheet at the effective date. There was a discussion about the existing resources available on the implementation portal of the FASB website that includes a variety of resources that could be leveraged to help companies transition to the new standard.

The PCC members and FASB staff later engaged in a discussion specific to revenue implementation. During that discussion, PCC members specified that variable consideration and disclosures are two complex areas that could benefit from additional educational resources. One PCC member indicated that a robust disclosure example would be helpful. One Board member observed that private companies are given additional time to adopt the standard with the intention that they are able to look to the public companies in their industry as an example. FASB staff further stated that revenue recognition disclosure requirements are intended to involve judgment and that they don't want to limit the judgment by providing a specific example. FASB staff concluded the conversation on revenue by indicating a desire to refresh the existing website content centered around many of the issues in question.

As part of a more general implementation discussion, a Board member asked PCC members about the current status of private company implementation efforts. Multiple PCC members indicated that many private companies have not yet started to implement the leasing standard because they are still concentrating on the implementation of Topic 606. A PCC member observed that it is not unusual for private companies to delay implementation efforts of new accounting standards until they approach the effective date. However, that member pointed out that many private companies with complex leasing arrangements have already begun implementation.

In response to comments from PCC members indicating a varying level of awareness from certain private company stakeholder groups, a Board member suggested providing stakeholders with additional education (perhaps through a webcast) about the expected impact on financial reporting from Topic 842 and Topic 606. Another Board member highlighted that a significant amount of educational information has already been produced by the FASB and is easily accessible on the implementation portal of the FASB website.

Distinguishing Liabilities from Equity (Including Convertible Debt)

The FASB staff began by explaining the simplifications in accounting for convertible debt and convertible preferred shares that the project is pursuing. One PCC member inquired as to whether any companies are disadvantaged by the decrease in models, and a Board member responded that the Board has not received any such feedback. FASB staff highlighted that the simplified accounting for convertible instruments would provide a more simple and straight-forward starting point for users to perform their analysis. Because of the comprehensive disclosure requirements, no information is expected to be lost.

The FASB staff then described the derivatives scope exception by focusing on three major proposed changes to GAAP, including consideration of probability when evaluating the indexation and settlement criteria, elimination of three of the seven conditions for equity classification under the settlement criterion, and reassessment only upon triggering events.

The FASB staff highlighted a single additional disclosure for the derivatives scope exception, which would require entities to identify triggering events that could cause a reclassification. One PCC member expressed concerns with the clarity of the disclosure requirement and indicated that it seemed like a "laundry list" of potential triggering events would have to be provided (depending on whether a threshold is considered in making the determination). FASB staff noted that its intention is not to have a boiler plate disclosure and that the exposure draft will solicit feedback on that same question in order to ensure the resulting disclosure is beneficial for users.

The conversation concluded with a discussion of the relationship between the project and the FASB Conceptual Framework. One PCC member commented that the project provided practical and sensible conclusions but questioned whether the project aligns with the conceptual definition of a liability. The FASB staff indicated that it gave primacy to the objective of financial reporting and expected that the proposed changes would provide more relevant information to users in making decisions about providing resources to an entity. Overall, PCC members supported the reduction in the number of models and the general simplification objective of the project.

Disclosures by Business Entities about Government Assistance

The FASB staff provided an update on the project and shared some of the feedback that was received during the external review of the staff draft. Stakeholders requested clarification of certain aspects of the document including scope. Larger public company preparers raised concerns about the cost and complexity that could be involved in complying with the disclosures. Preparers indicated that current systems were not capable of capturing the information that would be necessary for the required disclosures. PCC members who represent users voiced support for the proposed disclosures. One PCC member indicated that the duration of an agreement is typically not readily available and that disclosure about the terms and conditions of an agreement can be useful to understand when the receipt of government assistance may cease. Other PCC members indicated that information about government assistance is generally available from other sources and questioned the need for disclosure in the financial statements. One PCC member noted that of the small group of professionals he polled (roughly 30 individuals who are actively involved with M&A transactions and consist of investment bankers, attorneys, and auditors), government assistance was not prevalent and, therefore, disclosures about government assistance for private companies are not necessary. However, other PPC members disagreed and expressed their observation that they frequently see arrangements relating to government assistance and noted that there is an increasing number of them. The FASB staff highlighted that feedback from various sources indicates that this information would be useful. In response to a question from one PCC member, the FASB staff noted that the scope of the project has been narrowed from the exposure draft in response to stakeholder feedback.

Financial Performance Reporting—Disaggregation of Performance Information

The FASB staff provided an update on the outreach that was performed during the fall of 2018. During outreach, the staff tried to understand challenges related to disaggregating functional line items by natural components. The staff heard from stakeholders that the number and variety of accounting and reporting systems complicates the consolidation process. Both systems and the process of allocations prevent systems from disaggregating cost of revenues and selling, general, and administrative expenses by natural components because information is summarized throughout the consolidation process. That results in a loss of decision-useful information at more granular levels. Then the staff explained how the identification of those challenges helped to develop an internal view approach, which seeks to disaggregate performance information based on how it is internally viewed by management. Several PCC members identified challenges with this approach because management may review line items that may be unique to their entity and those line items may change over time. Those members noted that this approach may not lead to comparable information and requiring those disclosures may cause competitive harm; however, PCC members noted that trend information within an entity would be available from this approach. One PCC member suggested that the staff conduct additional outreach with financial statement users to understand what information would help create meaningful financial statement analysis. Several PCC members from a user perspective stated that disaggregation of the income statement would be useful in predicting future cash flows. Another PCC member noted that bifurcating the information could provide more decision-useful information particularly as it relates to consolidations and mergers in order to understand what information is consolidated into line items on the income statement.

Simplifying the Balance Sheet Classification of Debt

FASB staff explained the background of the project, highlighting the objective to reduce the cost and complexity associated with determining whether debt should be classified as a current or noncurrent liability. Specifically, the staff discussed replacing the narrow-scope, fact-specific guidance that currently exists with an overarching principle for determining debt classification.

FASB staff focused much of the discussion on unused financing arrangements. Stakeholders previously raised an issue about how the classification principle should be applied to situations in which there is a debt arrangement and an unused financing arrangement. The staff provided the following example—a variable rate demand obligation with a remarketing agreement in which a remarketing agent will use its best efforts to remarket the debt when the bondholder demands repayment of that debt. Additionally, a long-term financing arrangement such as a letter of credit is in place to provide liquidity in connection with that debt in the event the remarketing efforts are unsuccessful. The Board members have been considering whether the existence of an unused long-term financing arrangement should influence the classification of a debt arrangement.

At its September 2017 meeting, the Board decided that if a long-term financing arrangement is in place as of the balance sheet date, the amount of current maturities for any other debt arrangements would be reduced by the unused amount of the long-term financing arrangement and classified as a noncurrent liability. When brought to the PCC previously, that decision was met with general disapproval. At its August 2018 meeting, the Board reversed its decision and decided that an unused long-term financing arrangement in place at the balance sheet date should be disregarded in determining the classification of debt. The PCC members continued to express support for that decision.

Disclosure Framework: Disclosure Review—Income Taxes

The FASB staff provided a project update on what has occurred since the October 2018 PCC meeting. The staff began by discussing proposed disclosures that would affect all entities. The staff explained that the proposed Update also would include a private-company-specific disclosure that would require an entity other than a public business entity to disclose the amount of federal, state, and foreign tax credit carryforwards and the non-tax-effected amount of other federal, state, and foreign carryforwards. PCC member feedback indicated that non-tax-effected carryforwards would be less costly to disclose and that users would find this information useful.

One disclosure in the proposed Update would require all entities to disaggregate income tax expense (or benefit) and income taxes paid between federal, state, and foreign amounts. Several PCC members noted that separately disclosing state tax expense would be costly because many entities do not calculate income tax expense at that level of granularity in their income tax provision. PCC members explained that they estimate their taxes using a federal/state blended rate instead of calculating an exact state income tax expense. The FASB staff asked PCC members whether they could use the estimated rate to determine the state tax expense because the federal tax rate is static. PCC members said that they could use that rate but that it would require a more precise true-up in the return-to-provision calculation in the following year. Today, an entity can offset true-ups to its federal and state tax expense, whereas they would not be able to do so under the proposed disclosure. The FASB chairman noted that by requiring additional disaggregation, audit costs could increase because auditors would need to focus on auditing two separate calculations. One PCC member noted that the disclosure may be difficult because of progressive corporate tax rates at the state level. A Board member questioned whether the complexity was due to a combination of those progressive rates and doing business in multiple states. The FASB chairman suggested potentially not requiring the proposed disaggregation disclosures for private companies. Several PCC members noted that users could obtain that information through their access to management and related tax returns, if needed.

Disclosure—Codifying SEC Disclosures

The FASB staff explained the overall premise of the project and shared an overview of the Securities and Exchange Commission's referred disclosures affecting private companies. The FASB staff specifically highlighted the change to the debt disclosure, which would require private companies to disclose the weighted-average interest rate associated with outstanding short-term borrowings. The staff noted that feedback from the PCC in December 2018 indicated that the disclosure could be costly to provide and PCC members who are users indicated that they can estimate it, but the Board decided to include the disclosure due to the decision-useful information provided by the disclosure when short-term borrowings fluctuate significantly during the period. One PCC member suggested that the calculation could be complex and may not be cost beneficial. Another PCC member questioned whether the London Interbank Offered Rate (LIBOR) transition will affect the calculation, to which the FASB staff indicated that it will not because the weighted-average interest rate is based on the actual interest expense charged.

Various PCC members asked clarifying questions about the proposed changes to disclosures relating to interim periods, preferred shares, assets subject to liens, and consolidations. The

FASB staff provided clarification to address the timing concerns expressed by PCC members by indicating that one of the interim period disclosures is a clarification of the requirement today to disclose a change in reporting entity in the period of change and the other interim period disclosure requires an entity to disclose information about combined entities that is readily available. One PCC member expressed concern with the operability of disclosing separate results of combined entities under common control, and the FASB staff further clarified that separate results would be known prior to the combination and should not result in significant additional costs. The FASB staff highlighted that the change to the disclosures for preferred shares is minor and is intended to simplify the language by removing the judgment that is currently required. The FASB staff also explained that the disclosures for assets subject to lien are currently narrow and targeted and the proposed change would be broader and more comprehensive. For the change to the consolidation disclosures, several PCC members questioned why it would be useful to disclose the name of the entity newly included in the consolidation because an entity could have many subsidiaries. The FASB staff responded that one Board member also raised a similar concern and that there will be a question in the proposed Update about requiring that disclosure for private companies. Overall, the FASB staff clarified that many of the disclosure amendments are intended to be simplifications and are not wholesale changes to what is currently required under GAAP.