SMALL BUSINESS ADVISORY COMMITTEE

FASB Offices: Norwalk, Connecticut

April 30, 2013
Agenda*
Meeting Chair: Jeff Mechanick, FASB Assistant Director

8:00 – 8:55 am	**(Optional) Educational Session for SBAC Members:**
(55 minutes)	FASB Projects on Accounting for Financial Instruments and Leases (1 CPE will be available to attendees that are CPAs)
9:00 am	**Advisory Meeting Begins**
9:05 – 10:00 am	**Topic 1: Status Update Reports**

(55 minutes)	• Report of the FASB Chairman (Leslie Seidman)
	• Report on Private Company Activities (Daryl Buck)
	  ○ Decision-making Framework, including an update about changes to the "industry-specific" notions
	  ○ Recognition and measurement of various identifiable assets acquired in a business combination
	  ○ Definition of a nonpublic entity – FASB's consideration of what constitutes a "public market"
	  ○ PCC Agenda Request on Development Stage Entities
	• Update from the AICPA (Dan Noll)
	  ○ Activities of the Auditing Standards Board
	  ○ Recent AICPA guidance on the valuation of private equity firms

10:00 – 10:30 am	**Topic 2: Pushdown Accounting for Private Entities**
(30 minutes)	*Session Objective:* *To discuss SBAC members' views about the direction of the EITF on this issue.*
10:30 – 10:45 am	**BREAK** *(15 minutes)*
10:45 am – 12:00 pm	**Topic 3: Accounting for Financial Instruments**
(75 minutes)	*Session Objective:* *To discuss SBAC members' views about the proposal, focusing on (1) whether financial institutions have a different or similar view than other small businesses and (2) the costs and benefits of implementation of the proposal from a small business perspective.*

12:00 pm – 12:30 pm	**Topic 4: Leases**
(30 minutes)	*Session Objective: To discuss SBAC members' preliminary views on the forthcoming Exposure Draft and to answer any questions that SBAC members' have to help facilitate input and responses from the broader small business community.*
12:30 – 1:30 pm	**LUNCH** *(60 minutes)*
1:30 – 2:00 pm *(30 minutes)*	**Topic 5: Accounting for Stock Compensation (Pre-agenda research)** *Session Objective: To discuss SBAC members' views about the need for improvement in the accounting for stock compensation and the prevalence of certain issues for both public and private small businesses. (SBAC members have been asked to participate in a very brief survey on this topic prior to the meeting)*
2:00 – 2:45 pm *(45 minutes)*	**Topic 6: Revenue Recognition (Implementation Plan)** *Session Objectives:* *To discuss the FASB's plan to identify and potentially address implementation issues associated with their priority projects, focusing on the FASB's forthcoming standard on revenue recognition.* *To solicit SBAC members' input about the suitability and sufficiency of that plan in a small business context.*
2:45 – 3:00 pm *(15 minutes)*	**Topic 7: Potential Implications of Emerging Trends on Financial Reporting Standards** *Session Objective:* *To discuss any recent and emerging small business trends with possible financial reporting implications (SBAC members). SBAC members will be asked whether they are aware of any accounting implications related to the Affordable Care Act.*
3:00 pm	**ADJOURNMENT**

* Times are approximate.

REPORT OF THE FASB CHAIRMAN

TO THE FINANCIAL ACCOUNTING FOUNDATION

October 1, 2012 through December 31, 2012

ITEM 1: TECHNICAL ACTIVITIES

BOARD AND STAFF ACTIVITIES

a. The following Accounting Standards Updates were issued:

1. Accounting Standards Update No. 2012-05, *Statement of Cash Flows (Topic 230): Not-for-Profit Entities: Classification of the Sale Proceeds of Donated Financial Assets in the Statement of Cash Flows* (a consensus of the FASB Emerging Issues Task Force) (issued October 2012)
2. Accounting Standards Update No. 2012-06, *Business Combinations (Topic 805): Subsequent Accounting for an Indemnification Asset Recognized at the Acquisition Date as a Result of a Government-Assisted Acquisition of a Financial Institution* (a consensus of the FASB Emerging Issues Task Force) (issued October 2012)
3. Accounting Standards Update No. 2012-07, *Entertainment—Films (Topic 926): Accounting for Fair Value Information That Arises after the Measurement Date and Its Inclusion in the Impairment Analysis of Unamortized Film Costs* (a consensus of the FASB Emerging Issues Task Force) (issued October 2012).

b. The following Exposure Documents were issued:

1. Proposed Accounting Standards Update, *Foreign Currency Matters (Topic 830): Parent's Accounting for the Cumulative Translation Adjustment upon Derecognition of Certain Subsidiaries or Groups of Assets within a Foreign Entity or of an Investment in a Foreign Entity* (a consensus of the FASB Emerging Issues Task Force) (issued October 11, 2012). Comment deadline: December 10, 2012
2. Proposed Accounting Standards Update, *Consolidation (Topic 810): Accounting for the Difference between the Fair Value of the Assets and the Fair Value of the Liabilities of a Consolidated Collateralized Financing Entity* (a consensus of the FASB Emerging Issues Task Force) (issued October 11, 2012). Comment deadline: December 10, 2012
3. Proposed Accounting Standards Update, *Balance Sheet (Topic 210): Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities* (issued November 26, 2012). Comment deadline: December 21, 2012
4. Proposed Accounting Standards Update, *Financial Instruments—Credit Losses (Subtopic 825-15)* (issued December 20, 2012). Comment deadline: April 30, 2013.

c. The following projects were added to the FASB's technical agenda:

1. Balance Sheet Offsetting—Scope Clarification of Accounting Standards Update No. 2011-11 (October 2012)
2. Nonpublic Entities—Clarification of a Fair Value Disclosure Requirement (December 2012)
3. The following issues were added to the EITF's agenda in November 2012:
   a. Issue No. 13-A, "Inclusion of the Fed Funds Effective Swap Rate as a Benchmark Interest Rate for Hedge Accounting Purposes"
   b. Issue No. 13-B, "Accounting for Investments in Tax Credits"
   c. Issue No. 13-C, "Presentation of a Liability for an Unrecognized Tax Benefit When a Net Operating Loss Carryforward or Tax Credit Carryforward Exists."

d. No projects were removed from the FASB agenda before their completion.

e. Meetings of FASB Standing Advisory Groups:

1. Financial Accounting Standards Advisory Council (FASAC):
   a. All Board members and several FASB staff members participated in the October 2012 meeting of the FASAC. Council members discussed the reasons non-GAAP measures are used and continued their discussion about the FASB's approach to evaluating costs and benefits.
   b. All Board members and several FASB staff members participated in the December 2012 meeting of the FASAC. Council members discussed the development of a comprehensive FASAC survey on priorities that will be conducted in 2013 and their views about transition, the implications and preparation for transition for preparers and users, and implementation guidance related to the FASB's project on revenue recognition.
   c. FASB members and FASB senior staff met with the FASAC chairman to discuss recommendations arising from his review of the structure and operation of the FASB's advisory groups. The FASB chairman expects to study those recommendations and coordinate with the FAF to develop an implementation plan in the first quarter of 2013.
2. All Board members and several staff members participated in the December meeting of the Private Company Council (PCC).
3. Investors Technical Advisory Committee (ITAC):
   a. Six Board members and several FASB staff members met with the ITAC in November 2012. Matters discussed included the projects on the accounting for financial instruments, disclosure framework, and going concern. Committee members also discussed current revenue recognition and segment disclosures.

f. Advisory Group Membership Changes:
1. Three ITAC members completed their terms on December 31, 2012— Mark LaMonte, Elizabeth Mooney, and Mark Newsome. New candidates will be considered for appointment in the first quarter of 2013.

g. Outreach Activities—Meetings with Industry or Other Representative Groups:

1. IMA's Small Business Regulatory and Financial Affairs Committee (SBC). One Board member and several FASB staff members participated in a closed meeting (conference call) with IMA's SBC. Matters discussed included private company accounting initiatives, including the Private Company Council, and the FASB's process for considering and reviewing comment letters.

2. American Gas Association (AGA) and Edison Electric Institute (EEI). Two Board members and the FASB technical director met in a closed meeting with AGA and EEI members. Key discussion topics included the FASB's projects on leases, revenue recognition, and accounting for financial instruments. AGA and EEI members also provided an update on financial reporting implications of industry trends and changes.

3. Financial Executives Institute (FEI). A Board member participated in the quarterly meetings of FEI's Committee on Corporate Reporting.

h. Project-Specific Outreach Activities. The more significant project-specific outreach activities undertaken included:

1. *Impairment of financial instruments:* The Board and FASB staff continued outreach activities relating to the current expected credit loss model for impairment proposed in the Board's December 2012 Exposure Draft.
    a. The Board hosted an educational webcast to explain the proposed current expected credit loss model.
    b. Staff and Board representatives discussed the proposed model with the Private Company Financial Reporting Committee, ITAC, targeted financial institutions, financial institution regulators, and one of the major public accounting firms.
    c. FASB representatives also provided an educational overview of the proposed model to various financial analysts.

2. *Balance sheet offsetting:* FASB staff discussed issues arising from the implementation of the recently issued Accounting Standards Update on balance sheet offsetting in private meetings with a number of major financial institutions, financial institution representative groups (ISDA and SIFMA), and two of the major public accounting firms.

3. *Disclosure framework:* The Board and FASB staff continued outreach activities relating to the Invitation to Comment issued in July:
    a. The Board and the Center for Audit Quality sponsored two forums to discuss flexible disclosure requirements, reporting entity discretion in identifying appropriate disclosures, and the overlap between SEC requirements and FASB requirements. The invited participants included financial statement preparers, users, and auditors, as well as attorneys and regulators.
    b. A Board member and an FASB staff member attended outreach events sponsored by EFRAG at which both the EFRAG Discussion Paper on disclosures and the FASB Invitation to Comment were discussed.

4. *Going concern:* Board and FASB staff representatives met with representatives of the SEC, PCAOB, and ASB to coordinate development of proposed changes to this area. The project was also discussed with ITAC, the FASB's Private Company Council, the CAQ's Task Force on Going Concern, and the AICPA's Technical Issues Committee.
5. *Insurance contracts:* The Board and FASB staff continued outreach activities in connection with the development of an Exposure Draft on accounting for insurance contracts:
    a. Board and staff representatives discussed the project with users at a Columbia Business School-sponsored roundtable and other meetings with investors.
    b. Board and staff representatives discussed the project with representatives of a wide variety of insurance companies through industry conferences and roundtables sponsored by two of the major accounting firms and other meetings.
6. *Leases:* The FASB staff discussed the leasing proposal with ITAC, the PCFRC, representatives of the National Association of Real Estate Investment Trusts, and two of the major public accounting firms.
7. *Not-for-profit financial reporting: financial statements:* The FASB staff conducted outreach to better understand user information needs, meeting with representatives of the major credit rating agencies and other users.
8. *Accounting for repurchase agreements:* The FASB staff continued its outreach activities, discussing various technical and practical issues with major financial institutions, the four major public accounting firms, and representatives of the PCAOB.
1. *Revenue recognition:* Representatives of the Board and FASB staff continued outreach activities to inform the redeliberations of the 2011 Exposure Draft issued jointly with the IASB:
    a. Staff members discussed a variety of technical issues with representatives of the SEC.
    b. Workshops were held in New York, Tokyo, and London to discuss proposed disclosure requirements with preparers and financial statement users.
    c. Staff discussed technical and practical issues with representatives of the construction, aerospace and defense, asset management industries, and various other individual companies.

COLLABORATION WITH THE INTERNATIONAL ACCOUNTING STANDARDS BOARD

a. The FASB and the IASB held several multi-day joint Board meetings by video conference.

b. The FASB and the IASB held private, small-group video-conference meetings on the joint revenue recognition project.

c. The FASB and the IASB directors met periodically to discuss technical and administrative matters.

OTHER INTERNATIONAL ACTIVITIES

a. The FASB chairman and a Board member participated in the IFASS National Standard Setters meeting in Zurich.

b. An FASB Board member participated in the World Standard Setters meeting in London.

c. An FASB Board member participated in the EFRAG Disclosure Framework meeting in Amsterdam.

d. The FASB/IASB Financial Reporting Issues Conference was held in Norwalk.

XBRL ACTIVITIES

The FAF is responsible for the ongoing development and maintenance of the U.S. GAAP Financial Reporting Taxonomy (UGT) applicable to public issuers registered with the SEC. The FAF has delegated these responsibilities to the FASB.

a. Technical activities:
    1. In December 2012, delivered the 2013 US GAAP Financial Reporting *Taxonomy* (UGT) and supporting collateral to SEC as final, posting it to the website as final pending SEC acceptance.
    2. Developed a revised calculation hierarchy for the UGT for publishing as beta in first quarter 2013.
b. Outreach activities included the following:
    1. A conference call with the FASB Taxonomy Advisory Group (TAG). The TAG includes participants from preparers, CPA firms, service providers, data aggregators, and analysts. This advisory group provides valuable input on the changes and directions taken with each taxonomy release.
    2. Twice monthly conference calls with the XBRL Insurance Working Group to facilitate taxonomy improvements for the insurance industry.
    3. Monthly XBRL US Best Practice conference calls.
    4. A private meeting of FASB Board and staff members with representatives of Bloomberg (data aggregator) to learn about their requirements for XBRL tagged data and how they collect and use financial information.
c. Educational efforts: FASB XBRL staff wrote several articles and spoke at a variety of conferences.
d. Other XBRL activities:
        1. XBRL staff participated in IASB XAC and XQRT Meetings in London, providing input and guidance for the IFRS taxonomy effort. XBRL staff met with China Banking Regulatory Commission representatives to share

our experience with the ongoing development and maintenance of the UGT.
2. FASB staff participated in the first meeting and a following meeting (December 12, 2012) of an NFP industry working group focused on developing a NFP taxonomy built off of the UGT.

ITEM 2: EDUCATION AND COMMUNICATIONS

EDUCATIONAL WEBCASTS AND PODCASTS DELIVERED

a. The FASB hosted the following educational webinars:

1. IN FOCUS: The FASB Private Company Decision-Making Framework Project
2. IN FOCUS: Accounting for Credit Losses on Financial Instruments
3. IN FOCUS: FASB Update for Nonpublic Entities.

b. Podcasts:

1. FASB Member Tom Linsmeier Provides an Overview of the FASB's Proposed Standard to Improve Accounting for Credit Losses on Financial Assets.

SPEECHES DELIVERED

FASB members or staff delivered speeches at the following conferences and events:

- AAA Northeast Regional Meeting
- AAA/Bryant University Northeast Conference
- ACLI Annual Conference
- ACPEN Not-for-Profit Accounting and Tax Update
- AGC Construction Financial Management Conference
- AICPA National Conference on Credit Unions
- AICPA National Construction Industry Conference
- AICPA National Governmental & Not-for-Profit Training Program
- AICPA National Healthcare Industry Conference
- AICPA SEC & PCAOB Conference
- AICPA SIFMA National Conference on Securities Industry
- Baruch College Emanuel Saxe Distinguished Lecture in Accountancy
- BNA Bloomberg Webinar
- Bryant University Annual XBRL Conference
- College of William & Mary Master of Accounting Program
- Duquesne University Master of Accountancy Program
- ELFA Annual Convention
- Ernst & Young Accounting Change Symposium
- FDIC 6th Annual Accounting & Auditing Conference
- Federal Reserve Board Accounting Communications Network Fall Meeting
- FEI 31st Annual Current Financial Reporting Issues

- FEI Seattle/Washington State Chapter Meeting
- ICI Tax & Accounting Conference
- IMA Hartford Chapter
- Institutional Investor's US Institute CFO Forum
- KPMG Global FR and Valuation Conference
- Missouri Society of CPAs Not-for-Profit Conference
- Mortgage Bankers Association 2012 Accounting & Financial Management Conference
- NACD 2012 Board Leadership Conference
- Nexia International Audit Forum Meeting
- NJCPA Non-Profit Conference
- NYSSCPA Foundation for Accounting Education
- NYSSCPA IFRS Conference
- Oklahoma State University 12th Annual Accounting & Financial Reporting Conference
- The SEC Institute 28th Annual SEC Reporting & FASB Forum
- The SEC Institute SEC Reporting Conference
- South Carolina Association of CPAs 2012 Accounting & Auditing Conference
- United Way Worldwide 11th Annual United Way Financial Management and Human Resources Forum
- University of Florida/FICPA Accounting Conference
- University of Michigan
- University of New Orleans
- University of North Texas Professional Development Institute—Accounting & Financial Reporting Update Conference
- University of Oklahoma Professional Development Speaker Series
- Utah State Huntsman School Accounting Conference
- WSCPA Not-for-Profit Conference
- XBRL US XBRL and Corporate Actions Forum
- XBRL US Update on US GAAP Taxonomy

ITEM 3: ADMINISTRATIVE, PROCEDURAL, AND STRATEGIC ACTIVITIES

a. Administrative Matters:

1. Five Board members attended the November FAF Trustees meeting.
2. The FASB chairman developed a proposed 2013 operating budget, submitting it to the FAF Trustees for approval.

b. Professional Development—the following professional development sessions were presented to the Board and staff:

1. Application and Modeling of XBRL Financial Data. Louis Matherne, FASB Chief of Taxonomy Development; David Shaw, XBRL Assistant Project Manager, and Meredith Cheng, Project Research Associate, instructed

participants in how XBRL data are used and the interaction between XBRL data modeling and the standard-setting process. The session covered the application and modeling of XBRL Financial Data and included a demonstration of XBRL data in use.

2. Private Company Update. Michael Cheng, FASB Project Manager, and Liz Gagnon, FASB Project Manager, explained to participants the various private company initiatives under way at the FASB. The session included an overview of the newly established Private Company Council, the Board's Invitation to Comment describing a proposed decision-making framework for private companies, and tentative decisions reached in the Board's project to develop a definition of nonpublic entity.
3. Lessons Learned: Key Takeaways from Recent Company/Market Decline. Dan Mahoney, Global Head of CFRA.
4. XBRL staff attended a two-day data modeling workshop held at the FASB's offices.

ITEM 4: GOVERNMENT AND REGULATORY LIAISON ACTIVITIES

a. Members of the SEC, the PCAOB, Congress, and the Administration and their staffs were informed about the activities of the FASB through various meetings and other forums, including:

1. The FASB technical director and the FAF vice president provided input to the House Financial Services Oversight & Investigations Subcommittee regarding the November 2012 report of the Subcommittee's March 28, 2012 hearing on MF Global.

2. The FASB chairman, at least two FASB members, and the FASB technical director participated in a meeting regarding Congressional and Administration activities important to the FASB (closed meeting).

3. The FASB chairman, an FASB Board member, the FASB technical director, and the FAF vice president participated in the quarterly meeting with the financial institutions regulators.

4. An FASB member met privately with representatives of the Office of the Comptroller of the Currency.

5. The FASB chairman met with members of the Financial Stability Board Steering Committee (including the IASB chairman) to discuss progress on the project on the accounting for financial instruments (closed meeting).

6. The FASB chairman and a staff member participated in a meeting with international bank regulators, financial institutions, IASB Board and staff members, and an SEC staff member to discuss projects relating to the financial services industry (closed meeting).

b. An FASB member participated as an observer in the semi-annual meeting of the PCAOB's Standards Advisory Group.

ITEM 5: OTHER COMMUNICATIONS ACTIVITIES

a. The FASB issued the following press releases/media advisories/Tweets:

1. Register Today for the FASB's "Encore" CPE Webcast on the Private Company Decision-Making Framework Project on October 18
2. Newly Created Private Company Council to Hold Inaugural Public Meeting on December 6
3. Registration Opens for November 9 Webcast, *IN FOCUS: Accounting for Credit Losses on Financial Instruments*
4. FASB Extends Invitation to Comment on Private Company Decision-Making Framework Staff Paper to November 9
5. FASB Extends Disclosure Framework Comment Period to November 30
6. FASB Statement on Financial Stability Board's Report on Bank Risk Disclosures
7. FASB Issues Proposal to Clarify Scope of Disclosures That Apply to Balance Sheet Offsetting of Assets and Liabilities
8. Financial Accounting Foundation Appoints Four New Members to the Financial Accounting Standards Advisory Council
9. Registration Opens for December 13th CPE Webcast *IN FOCUS: FASB Update for Nonpublic Entities*
10. Private Company Council Holds Inaugural Meeting, Identifies Four Areas for Study
11. Report on First PCC Meeting to Be Featured in December 13 Webcast, *IN FOCUS: FASB Update for Nonpublic Entities*
12. FASB and Center for Audit Quality Issue Forum Observations Summary on Disclosure Effectiveness
13. FASB to Webcast Technical Forum for Continuing Professional Education Providers
14. FASB Proposes Improvements to Accounting for Credit Losses on Financial Assets
15. U.S. GAAP Financial Reporting Taxonomy Now Available.

b. The FASB issued "FASB in Focus" documents for the following:

1. Proposed Accounting Standards Update—*Financial Instruments—Credit Losses (Subtopic 825-15)*

c. Media Outreach:

1. During the quarter ended December 31, 2012, members of the FASB or its staff participated in numerous interviews with media.

ITEM 6: GASB LIAISON ACTIVITIES

a. GASB and FASB meeting minutes were shared with the FASB and GASB directors.

b. The GASB and FASB directors met monthly to discuss their technical agenda projects and other matters of mutual interest. The FASB and GASB chairmen and their respective directors held their quarterly meeting to discuss technical issues and other matters of mutual interest.

c. The GASB staff distributed a draft of GASB Statement No. 69, *Government Combinations and Disposals of Government Operations,* to the FASB for review.

d. The FASB staff distributed the following drafts for the GASB's review:

1. Proposed Accounting Standards Update, *Balance Sheet (Topic 210): Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities*
2. Proposed Accounting Standards Update, *Financial Instruments—Credit Losses (Subtopic 825-15)*
3. Proposed Accounting Standards Update, *Financial Instruments (Topic 825): Clarifying the Scope and Applicability of a Particular Disclosure to Nonpublic Entities*
4. Proposed Accounting Standards Update, *Transfers and Servicing (Topic 860): Reconsideration of Effective Control for Agreements That Entitle and Obligate the Transferor to Repurchase or Redeem Transferred Financial Assets and Accounting for Repurchase Financings.*

ATTACHMENT 2

Recognition of New Accounting Basis (Pushdown) in Certain Circumstances
(EITF Issue 12-F)
SBAC Meeting
April 30, 2013

Introduction

1. Current U.S. GAAP offers limited guidance for determining when, if ever, the cost of acquiring an entity should be used to establish a new accounting and reporting basis (pushdown) in the acquired entity's separate financial statements. SEC Staff Accounting Bulletin Topic No. 5.J, *New Basis of Accounting Required in Certain Circumstances*, EITF Topic No. D-97, "Push-Down Accounting," and other comments made by the SEC Observer at EITF meetings (which are codified in paragraphs 805-50-S99-1 through S99-4), provide guidance for SEC registrants on the pushdown basis of accounting. Additionally, certain financial institutions are required by their regulators to apply pushdown accounting in certain circumstances. The SEC staff's guidance indicates that if a purchase transaction results in an entity becoming substantially wholly owned, its standalone financial statements should be adjusted to reflect the basis of accounting of the acquirer. The SEC staff's guidance further states that pushdown accounting is (a) required when 95 percent or more of an entity's ownership is acquired, (b) permitted when 80 to 95 percent is acquired, and (c) prohibited when less than 80 percent is acquired. The existence of other interests, such as public debt, preferred stock, or a significant noncontrolling interest, however, may affect the acquired entity's ability to adjust its standalone financial statements to reflect the acquirer's basis of accounting. The SEC staff's guidance also indicates that holdings of investors who both mutually promote the acquisition and collaborate on the subsequent control of the acquired entity should be aggregated for the purpose of determining whether the acquired entity has become substantially wholly owned.

2. Since the SEC staff's guidance is only mandatory for SEC registrants, diversity in practice exists on the application of pushdown accounting by entities that are not SEC registrants. In addition, comparability issues have arisen due to the option in the SEC guidance to apply pushdown accounting when between 80 and 95 percent of an entity has been acquired. The FASB staff also notes that there are a significant number of practice issues that continue to arise on the application of pushdown accounting as a result of the limited guidance, including the absence of a basis for conclusions and a principle for when pushdown accounting should be applied.

Issue

3. The issue is whether a reporting entity should establish a new accounting basis in its standalone financial statements as a result of a transaction or other event in which an acquirer obtains a controlling financial interest in the reporting entity, and, if

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so, the resulting level of controlling ownership at which the new accounting basis should be required.

January/March 2013 EITF Discussion

4. The Task Force discussed the following three alternative views regarding the application of pushdown accounting and expressed a preference towards requiring pushdown accounting:

View A: A new accounting basis should be established when an acquirer obtains substantially all of the controlling financial interest in the reporting entity and thereby obtains control over the form of ownership of the reporting entity.

View B: A new accounting basis should be established when an acquirer obtains control of the reporting entity.

View C: A new accounting basis should not be established in an acquired entity's separate financial statements.

5. The Task Force discussed the feedback received from users of both public and nonpublic entity financial statements and the PCC that indicated mixed views on whether the new basis in the standalone financial statements of an acquired entity provides beneficial information for investment decision making. Some Task Force members indicated that the threshold for requiring pushdown accounting should remain high and should only be applied when there is a transaction, and, therefore, supported View A. Other Task Force members preferred a change-in-control threshold to apply pushdown accounting. Those Task Force members preferred a lower threshold because they believe that it would be operationally beneficial for both the acquiring entity and the subsidiary to not have to maintain two different sets of books. Additionally, one Task Force member noted that in determining the parent's accounting, a change in control is considered a significant event accounted for at fair value and pushdown accounting would align the accounting between the parent and subsidiary. Some Task Force members also commented that application of pushdown accounting to standalone financial statements of the acquired entity (subsidiary) would help users analyze its financial statements in the context of the financial statements of the acquirer (parent).

6. The Task Force concluded that the FASB staff should pursue development of a proposed model under which pushdown accounting could be optionally applied when an acquirer obtains control of a reporting entity. The Task Force will consider at a future meeting whether pushdown accounting should be made mandatory and, if the Task Force decides that it should be mandatory, then it will work to specify the threshold at which the application of pushdown accounting should be mandatory.

EITF Status

7. Further discussion is expected at a future EITF meeting.

Questions for Discussion

Question 1: What are your views on the direction of the EITF on this issue (see the conclusion in paragraph 6)?

Question 2:

(For preparers) Are there specific costs or operational concerns for small private companies with this direction that the Board/EITF should be aware of?

(For users) Do you have any additional insights about how the information would (or would not) benefit the users of the financial statements of small private companies that the Board/EITF should be aware of?

Question 3: Should pushdown accounting be mandatory for private companies or should it remain optional? If it should be made mandatory, what threshold should be used to make the guidance mandatory?

ATTACHMENT 5

Accounting for Stock Compensation (Pre-Agenda Research)
SBAC Meeting
April 30, 2013

In its February meeting, the Private Company Council (PCC) directed the FASB staff to develop a pre-agenda research memorandum on stock based compensation (Topic 718) *Compensation – Stock Compensation*.

To support the development of the stock-based compensation pre-agenda research memorandum, the FASB staff is conducting outreach to stakeholders to get their input on private company concerns, and recommendations for alternatives to the recognition, measurement and disclosure provisions of existing stock-based compensation guidance. The results of the research will assist the Board and the PCC in determining whether to put on its agenda a project related to stock-based compensation.

During a previous SBAC agenda call, participants supported the idea of soliciting information from SBAC members to help facilitate a discussion on various topics. Therefore, SBAC members were asked for their input on the following questions:

- Do you have concerns/recommendations about the accounting related to stock-based compensation? If so, please briefly describe them.
- Do those concerns/recommendations apply to solely private companies, or to both small public and private companies?

Brief History of Stock Based Compensation Accounting

1. APB Opinion No. 25, *Accounting for Stock Issued to Employees* (Opinion 25), was issued in 1972. Typically, no compensation cost was recognized in a company's financial statements using the intrinsic value[1] as prescribed by Opinion 25.
2. FASB Statement No. 123, *Accounting for Stock-Based Compensation* (SFAS 123), was issued in October 1995. SFAS 123 defined a fair value based method of accounting for stock based awards and encouraged all entities to adopt that method of accounting for their stock compensation plans. However, it also allowed an entity to continue to measure compensation cost for those plans using the intrinsic value based method as prescribed under Opinion 25. Pro forma disclosures were an alternative to financial statement recognition.

[1] Intrinsic value is defined as the amount by which the fair value of the underlying stock exceeds the exercise price of an option. Under Opinion 25, using the intrinsic value method, compensation cost is the excess, if any, of the quoted market price of the underlying stock at grant date over the amount an employee must pay to acquire the stock.

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3. FASB Statement No. 123 (revised 2004), *Share-Based Payment* (SFAS 123R) was issued in December 2004. SFAS 123R superseded APB Opinion 25 and was codified as ASC Topic 718, Compensation – Stock Compensation. As more fully described below, Topic 718 requires that the cost resulting from all share-based awards be recognized in the financial statements at fair value.

Current Stock Compensation Guidance under Topic 718 (in a nutshell)

4. An entity shall recognize the services received in a share-based payment transaction with an employee as services are rendered, generally beginning on the date the awards are granted.
5. An award must be evaluated as to whether it is an equity award or a liability award.
6. The share-based payment transactions with employees shall be measured based on the grant-date fair value (or in certain situations, a calculated value or intrinsic value) of the equity instruments issued or liabilities incurred.

    a) Fair value shall be measured based on the observable market price of an option with the same or similar terms and conditions, if one is available. For nonpublic entities, such market prices of an equity share option or similar instruments are frequently not available. If such market prices are not available, the fair value of equity and liability instruments shall be estimated using a valuation technique such as an option pricing model.

    b) If a nonpublic entity cannot reasonably estimate the fair value because it is not practicable for it to estimate the expected volatility of its share price, the entity shall use the calculated value method using a historical volatility of an appropriate industry index.

    c) Share-based awards for which it is not possible to reasonably estimate fair value at the grant date shall be accounted for based on its intrinsic value.

7. The compensation cost for an award of share-based employee compensation classified as equity shall be recognized in the income statement over the requisite service period, with a corresponding credit to equity (typically paid-in-capital). The fair value of an award classified as a liability shall be remeasured at the end of each reporting period through the settlement date. Changes in the fair value (or intrinsic value for a nonpublic entity that elects that method) of a liability award that occurs during the requisite service period shall be recognized as compensation cost over that period.

Feedback from SBAC Members

Below is a compilation of the responses received from SBAC members through April 23, 2013:

Private Company-Related Comments:

- I discussed with 3 owners of private companies. There seems to be little concern since stock is seldom if ever used to reward professional staff and the generational ownership transfer does not involve compensation.
- For private companies (non-publicly traded) and smaller companies (S-Corps), this is not a major concern since stock is usually held by the owners/family and relatives. Valuation becomes a problem when the company is sold or the stock is sold in the private market. I do not think stock based compensation is an issue for private companies.
- Forgetting the notion of public versus private for a moment, it seems to me that almost regardless of the form, compensation is compensation and needs to be accounted for as such. In my years of business in the construction business, I have never observed or heard of stock-based compensation. I doubt this is a huge issue in the private world.
- I do not have a concern about reporting stock based compensation (or other non-cash items).
- My primary concern in the accounting for stock-based comp involves the volatility calculation when measuring the FV of options. I have a small public company client with high volatility and the black scholes calculation of option value for an actual executive options grant was $1.30 per share; when the FV of the stock at grant date was $1.33 per share. It is ludicrous to think a marketplace participant would actually pay that. Accordingly, it represents a useless and possibly misleading amount, in my opinion.
- Determining fair value of stock for private companies and their certain securities (classes of common and preferred) can sometimes be challenging. The company's primary purpose in doing so is usually for compensation for tax purposes, where their "bias" is to be low. Accordingly, opposing objectives exist.
- It sometimes seems there is a lot of disclosure involving stock options; especially in circumstances where the share grants are not that material, either in number of shares or $ of compensation. You get the same 2+ pages, regardless of materiality. This would be an area for consideration of "scaling", as discussed with certain other disclosures. This comment could also apply to public companies, but perhaps is a more relevant comment for private companies.
- The primary concern with stock-based compensation for privately held companies is the valuation (which is pretty obvious). Many times the companies will use a valuation specialist to compute the value of the stock, but the assumptions, etc… that are used during the valuation are so numerous that the estimate of the value could be significantly different when computed by different valuation specialists. We are seeing more restricted stock being awarded to employees than options for 2012 and also more of our

clients are adopted ESOP plans to reward employees with company stock. The valuation issues are the same. Unsophisticated client accounting personnel also contribute to the complexity of accounting for stock based compensation in a private company. There is a tremendous amount of education that must take place when a private company implements a stock-based compensation plan.

- I tend to believe that this is more of a private company issue, however, the small accounting staff at a small public company would be similar to a private company's issues.
- When issuing awards classified as equity, ASC 718 prefers nonpublic companies to use the fair-value method. In the case of startups, it is a little more difficult to use fair-value...Even going to peer group public companies, it makes it difficult to estimate expected volatility. The alternative is to use calculated-value....which probably means valuations on grant dates or at the end of the reporting period. Adds a few more challenges and costs to the startup.
- NVCA's views over the years regarding accounting for stock based compensation are well known. But those concerns aren't related to the PCC's jurisdiction. The stock compensation accounting is part of a much larger (and sensitive) discussion. While disclosure relief for privates is worthwhile considering, measurement relief wouldn't be a priority because venture backed portfolio companies are on a track to go public.

Public Company-Related Comments:

- I am on the board of a small public company and management has no issue with the reporting.
- For a publicly traded company, the shareholders should know how their executives/staff/board members are being compensated. However, I think this information should be a footnote rather than a line on the financial statements. The question is how to value this compensation since public company stock is traded on open markets. How to determine the value is a concern unlike stock options which are granted with a specific value.

Other Comments:

- Cooperatives do not have stock as do investor owned corporations - the "stock" exists in the form of a certificate which is owned by each member of the cooperative. By operating on the not-for-profit basis - we allocate margins back to our members and - over time- return those margins to the member from whence it came. This essentially means that the member receives a return of capital as opposed to a return on capital.
- I would like "Cash Flows from Operations" highlighted more in the financial statements. Also, I have a general concern about the differentiation between public and private companies. I am not sure that distinction serves us best. Perhaps there should be a set of "basic" (cash basis, or something close to cash basis) principles that may be used when the users and issuer agree that nothing more is required.

Feedback Received from Other Stakeholders:

Below is a compilation of feedback received from various other stakeholders through April 22, 2013:

Private Company Comments:

Recognition

- Determining whether an award is a liability or equity award can be difficult. Some agreements contain terms with characteristics of both liability and equity awards.
- Repurchase features should generally not trigger liability accounting unless there is a pattern of redemption that would indicate cash settlement. If the terms of the award look like equity, then treat them as equity.
- For equity awards that will never monetize, recognition of stock compensation expense is less relevant. In certain circumstances, an equity award might not monetize until a change of control. Some stakeholders indicated in this situation, this is not a true expense to the private company; rather this would be a cost to the acquirer. Recording stock compensation expense could appear to reduce the financial position of the company if they never expect to settle the award by reducing assets of the company. Disclosures of the award terms without recognizing the expense would be sufficient.
- Some private companies view recognition of stock compensation expense to be a noncash expense and therefore, not relevant to the financial statements.
- From a lender's perspective, the recognition (and measurement) of a liability award is more important than an equity award. See measurement below.
- If the intent of the employee issued award is that when an employee terminates they will forfeit their options, then there may not be a reason to recognize an expense in the financial statements.

Measurement (Initial and Subsequent)

- Valuation of a private company's underlying stock can be difficult and costly. The difficulty is due to the lack of the private company stock being traded in an active market.
- Valuation of the stock option itself can be difficult and costly.
- Liability awards using the intrinsic value method have to remeasure the awards on an annual basis. As such, an annual valuation must be obtained which again, can be difficult and costly.
- Some lenders indicated that while they understand the difficulties and costs involved in valuing a private company, a valuation is a cost of doing business and issuing share-based awards.
- A nonpublic entity may not be able to reasonably estimate the fair value of its equity share options because it is not practicable for it to estimate the expected volatility of its share price because (1) there is no active trading market of the company's stock and (2) there is a lack of public companies comparable in which to use for the volatility calculation.

- If a nonpublic entity can't estimate the fair value of its equity share options, then it should account for its equity share options using calculated value using an appropriate industry sector index. There is a concern that industry sector indexes are not representative of the nature and operations of the private company and the Dow Jones Industry Index information is no longer readily available on the website.
- A practical expedient to calculating volatility would be welcome relief to private companies, but the practical expedient shouldn't materially diminish the estimated stock option value and thus, stock compensation expense.
- Other inputs to the option pricing model can be difficult to estimate when the company has no historical experience to assist in developing expectations about the future: (1) forfeitures (2) expected dividend rate (3) expected term.
- Some private companies stated that valuation firms don't always achieve a real understanding of their business, so they do not view the valuation report as a realistic indicator of what might be realized upon a liquidation event.
- An accurate measurement of a liability award is important to a lender. The lender is concerned about whether the settlement of the awards will have a significant impact and detrimental effect on the future cash flows, the ability of the private company to service the debt, cover other fixed charges, build reserve capacity and replenish assets in which to maintain and grow the business. Therefore, lenders indicate that accurate measurement, recognition, and disclosure of a liability award (stock compensation expense and the corresponding liability) is important.

Disclosure

- Streamlined disclosures about the options would seem more reasonable to private companies. There are typically a limited number of financial statement users and those users have direct access to management, if additional information is needed.
- From a lender's perspective, the disclosure of stock compensation expense and unrecognized stock compensation expense in a liability award is important and necessary for loan decision making purposes.

General

- Some private companies issue stock based awards because it is the savvy thing to do and also provides a recruitment tool for employees. This is particularly true in technology companies that are start-ups or smaller in size. These companies know little about the options and simply don't care about the accounting implications. In addition, some private companies don't expect to have a cash outlay until a change of control or liquidation. Due to the high costs of hiring service providers from a legal, valuation or an accounting (book or tax) perspective, the companies might cut corners in applying the provisions of the accounting guidance. The accounting implications of stock based awards do not become relevant until the negotiation phase of a sale of the company.
- Overall, the guidance can be onerous and difficult for a private company to interpret and apply on their own without significant help from their accounting,

tax and legal advisors. As such, private companies could incur a disproportionate burden of costs to account for stock options.

- Lenders indicated they would have direct access to management so if additional information was needed to aid in making a lending decision, the lender has that ability to request information from management.
- Overall, there can be more challenges in stock compensation accounting for private companies because of valuation difficulties and the wide variety of terms in stock based compensation award agreements.

Public Company Comments:

- Valuation of a public company's stock is relatively easier than a private company because the stock is being traded in an active market. It is a bit more difficult for a company that recently went public to have a more accurate valuation as there is limited historical trading activity.
- Public companies generally award stock options that are more basic in nature meaning the terms of the awards aren't complex compared to that of private equity groups or venture capital backed company awards issued.
- Inputs to option pricing models tend to be easier to estimate given there is historical experience except for in situations where the public company is a startup or recently became a public company.
- Public companies generally have more resources than private companies which facilitates the necessary time and attention to calculation of stock compensation.
- Public companies that issue a significant number of awards find the tracking of such awards to be time consuming and burdensome.

Questions for Discussion

Question 1: Based upon our discussion, what are your thoughts on the priority the PCC should assign to this topic?

Question 2: What other factors should the PCC consider is assessing whether to add a project to the agenda on accounting for stock compensation?