SEC, PCAOB and FASB update

Heather Dominey
November 12, 2018

Today's Agenda

- SEC update
  - Overview of the Commission and its priorities
  - Enforcement activities
  - Comment letters
- PCAOB update
  - Overview of the Board
  - Auditor's reporting model
  - Inspections – anticipated focus
  - Proposed auditing standards and projects
- FASB update
  - Recently issued FASB standards
  - FASB projects
  - Restatement themes

Learning objectives

- Identify key SEC initiatives, including strategic priorities under its current leadership
- Discuss SEC rules and other guidance that may require changes in reporting, disclosure or internal control processes
- Discuss the possible effects of recent PCAOB standard-setting activities
- Identify accounting standards issued in recent years that some companies may not have implemented yet that may be relevant to your financial reporting
- Identify the significant decisions by the FASB that may be relevant to your financial reporting

SEC update

EY

Overview of the Commission and its priorities

- SEC's current composition
  - Jay Clayton, SEC Chairman (Independent); Hester Peirce and Elad Roisman (Republicans); Robert Jackson and Kara Stein (Democrats)
- Strategic priorities
  - Capital formation – enhance the attractiveness of raising capital in public capital markets by reducing the regulatory burden on public companies
  - New accounting standards – monitor adoption of new standards
  - Cybersecurity – issue guidance and monitor disclosures about cybersecurity matters
  - ICOs and cryptocurrencies – monitor activity and enforce securities laws

EY

Capital formation
S-X Rule 3-13 relief

- Registrants may use relief available under Rule 3-13 to ask the SEC staff to modify or waive their SEC financial reporting obligations, based on the facts and circumstances, if such actions are consistent with investor protection
  - Registrants should consider requesting relief when Regulation S-X requires disclosures that are burdensome to generate but that may not be material to the total mix of information available to investors
  - Registrants must make a written request to the SEC staff, unless relief is self-executing according to the Financial Reporting Manual (FRM)
  - Otherwise, taking relief constitutes noncompliance with SEC rules

"I want to encourage companies to consider whether [Rule 3-13 relief] may be helpful in connection with their capital raising activities and assure you that SEC staff is placing a high priority on responding with timely guidance."

— SEC Chairman Jay Clayton

EY

Capital formation
Definition of smaller reporting company

- SEC amended the definition of a smaller reporting company (SRC) to allow more registrants to qualify for scaled disclosures
- Registrants may qualify as an SRC by meeting a revised public float test *or* a new two-part revenue/float test:

	Previous definition	Amended definition*
Public float	Public float of less than $75 million	Public float of less than $250 million
Revenue/float	Less than $50 million of annual revenues and no public float	Less than $100 million of annual revenues and public float of less than $700 million (including no public float)

* Existing registrants can only qualify using these thresholds during the first fiscal year ending after the rule becomes effective on 10 September 2018. In subsequent years, registrants that did not previously qualify as an SRC under the amended definition would be required to meet lower thresholds (i.e., 80% of the new threshold amounts).

Capital formation
Definition of smaller reporting company (continued)

- Registrants may omit financial statements of a significant acquired or to be acquired business for the earliest of the three years otherwise required if net revenues of that business are less than $100 million (up from $50 million)
- SEC did not raise the $75 million public float threshold in its accelerated filer definition
  - Accelerated filers that qualify as SRCs under the amended definition will remain subject to accelerated reporting deadlines and auditor attestation on internal control over financial reporting
  - SEC staff will make recommendations for possible changes to the accelerated filer definition

SEC estimates that 966 additional registrants will be eligible for SRC status in the first year under the new SRC definition.

— SEC Release No. 33-10513

Capital formation
Proposed amendments to S-X Rules 3-10 and 3-16

- Would streamline financial disclosure requirements for registered debt offerings involving subsidiary issuers or guarantors (S-X Rule 3-10) and affiliates whose securities are pledged as collateral (S-X Rule 3-16)
- Would narrow the circumstances in which Rule 3-10 would require separate financial statements by allowing subsidiary guarantor(s) to be less than 100% owned and *not* fully obligated for the debt
- Would streamline the Rule 3-10 disclosure requirements by:
  - Replacing condensed consolidating financial information with summarized financial information and expanded narrative disclosures
  - Reducing the periods that must be covered by the summarized financial information
  - Suspending the disclosures after a Form 15 filing
  - Eliminating the requirement to provide pre-acquisition guarantor financial statements under S-X Rule 3-10(g)
  - Allowing immaterial information to be omitted
- Would replace requirement to provide separate financial statements under Rule 3-16 with requirement to provide summarized financial information and narrative disclosures

Capital formation
Inline XBRL

- SEC adopted a final rule to require Inline XBRL tagging in financial statements and risk/return summaries for operating companies and mutual funds
  - Tags will be directly embedded in the HTML financial statements, rather than submitted in an exhibit to SEC filings
  - No change made to the scope of XBRL tagging
  - Rule does not require officer certification or auditor involvement similar to the current requirements
- Transition
  - Larger mutual funds (i.e., funds with net assets of $1 billion or more) and all other funds are required to use Inline XBRL tagging after 17 September 2020 and 17 September 2021, respectively
  - Operating companies filing as large accelerated, accelerated and non-accelerated filers (including foreign private issuers) are required to comply beginning with their first Form 10-Q for a fiscal period ending on or after 15 June 2019, 2020 and 2021, respectively

Capital formation
Disclosure update and simplification (DUSTR)

- SEC adopted a final rule that requires registrants to reconcile changes in stockholders' equity in Form 10-Q
- Eliminates or amends disclosure requirements that are redundant or outdated
  - Amendments are intended to simplify compliance, but are not expected to significantly change the information provided to investors
- Deletes disclosure requirements that overlap with US GAAP, including:
  - Ratio of earnings to fixed charges
  - Segment financial disclosures in the description of business section
  - Most accounting policy disclosures for derivatives
- Replaces the bright-line threshold (i.e., 25% of net assets) for providing disclosures about restricted net assets of subsidiaries with requirement to provide disclosures "when material"
- Effective on 5 November 2018

Capital formation
Ongoing rulemaking

- SEC's short-term rulemaking agenda includes items that are expected to promote capital formation
  - Final rulemaking stage: Fixing America's Surface Transportation (FAST) Act modernization and simplification of Regulation S-K
  - Upcoming proposals
    - Amendments to financial disclosure requirements for acquired businesses (S-X Rule 3-05 and Article 11)
    - Extending testing-the-waters provisions beyond emerging growth companies
    - Enhancing the effectiveness of business, financial and management disclosures required by Regulation S-K

New accounting standards

- Revenue from contracts with customers (ASC 606)
  - Revenue disclosures should be refined during the first year
  - Registrants that adopted the standard using the modified retrospective method may provide supplemental management's discussion and analysis using ASC 605 only during the year of transition
  - Registrants must conform an acquired entity's transition date and method to its own when preparing Article 11 pro formas – may request relief from the staff
- New leases (ASC 842) and credit losses (ASC 326) standards
  - SEC staff continues encouraging companies to stay focused
- SEC staff will focus on Staff Accounting Bulletin 74 disclosures, which should evolve over time as registrants make progress toward implementation of new standards
- Design, document and implement policies and procedures to make sound judgments
  - SEC staff stated that reasonable judgments will be respected

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Cybersecurity

- SEC release on cybersecurity disclosures is effective now
  - Reiterates much of the staff's 2011 disclosure guidance on cybersecurity
  - Expands guidance on materiality considerations and disclosures
  - Focuses on disclosure controls and procedures
  - Highlights importance of maintaining insider trading and Regulation Fair Disclosure (FD) policies that address cybersecurity
  - Reminds companies to provide disclosures tailored to their particular cybersecurity risks and incidents
- Division of Enforcement created a Cyber Unit to investigate and prosecute cyber-related cases, including matters involving non-timely disclosures of cyber incidents

"Issuers and other market participants must take their periodic and current disclosure obligations regarding cybersecurity risks seriously, and failure to do so may result in an enforcement action."

— SEC Chairman Jay Clayton

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ICOs and cryptocurrencies

- An initial coin offering that involves a security is subject to registration under the federal securities laws (e.g., Securities Act of 1933) unless eligible for exemption
  - Digital tokens are often securities because they involve an investment of money in a common enterprise with a reasonable expectation of profits to be derived from the entrepreneurial or managerial efforts of others (Howey test)
- Division of Corporation Finance has stated that Bitcoin does not implicate the securities laws, and current transactions in Ether are likely not securities transactions
- Simply labeling a digital asset as a cryptocurrency or utility token does not evade the SEC's registration requirements
- Cyber Unit is actively engaged in enforcement actions related to possible violations of federal securities laws involving ICOs and blockchain

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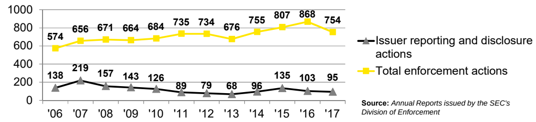
Enforcement statistics

- Total enforcement cases declined for the first time since 2013
  - SEC filed a total of 754 cases in 2017 (i.e., 13% decline)
    - 95 cases related to financial reporting and disclosures in 2017, down from 103 in 2016
  - Penalties and disgorgement dropped to $3.7 billion in 2017 from $4 billion in 2016



Source: *Annual Reports issued by the SEC's Division of Enforcement*

"While some [critics] point to particular statistics to claim that the SEC and more specifically Enforcement are pulling back their investor protection efforts, I want to make absolutely clear that is not the case."

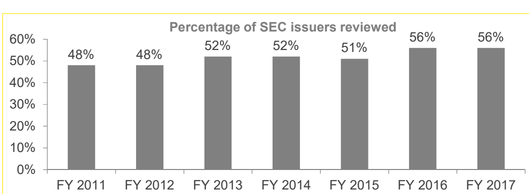
— SEC Chairman Jay Clayton

Enforcement activities

- Priorities of the Enforcement Division
  - Protect "Main Street" investors
  - Keep pace with technological changes (e.g., cybersecurity, ICOs, digital tokens)
  - Continue to enforce individual accountability to deter bad behavior
- Issuer accounting and disclosure issues
  - Fictitious revenue recognition
  - Improper capitalization of expenditures
  - Understatement of expenses and accrued liabilities
  - Overstatement of asset valuations
  - Misleading investors by overstating performance metrics
- Whistleblower program protects and rewards whistleblowers
  - SEC received more than 4,500 tips in fiscal 2017

The SEC's filing review process

- Review of periodic reports by Division of Corporation Finance at a minimum of every three years as mandated by the Sarbanes-Oxley Act
  - Many registrants reviewed more frequently

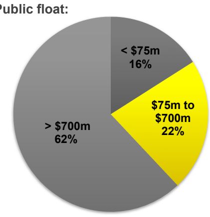


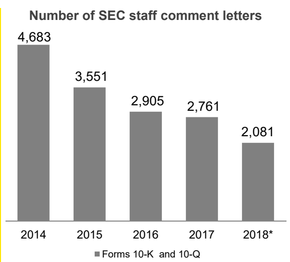
Source: SEC 2017 Annual Performance Report

The SEC's filing review process (continued)

Companies receiving comment letters by size

Public float:





Source: Audit Analytics – SEC UPLOAD comment letters issued related to Forms 10-K and 10-Q for the 12-month periods ended 30 June 2014 through 2018

* *The SEC staff publicly releases comment letters no earlier than 20 business days after completing its review. Therefore, some letters for the 12-month period ended 30 June 2018 may not yet be publicly available.*

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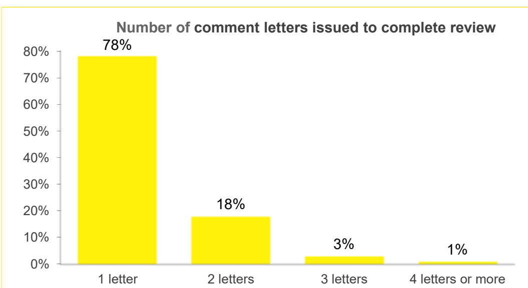
The SEC's filing review process (continued)



Source: Audit Analytics – Comment letters related to Forms 10-K posted to EDGAR during the 12-month period ended 30 June 2018

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Areas of frequent SEC staff comment

Comment letter topic	Ranking 2018	Ranking 2017
Management's discussion and analysis (MD&A)	1	2
Non-GAAP financial measures	2	1
Fair value measurements	3	3
Segment reporting	4	4
Revenue recognition	5	5
Intangible assets and goodwill	6	6
State sponsors of terrorism	7	8
Income tax	8	7
Acquisitions and business combinations	9	9
Contingencies	10	14

Source: Audit Analytics – Comment letter taxonomy for SEC staff comment letters issued to registrants related to Forms 10-K from 1 July 2016 to 30 June 2018

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Areas of frequent SEC staff comment (continued)
ASC 606, *Revenue from contracts with customers*

- SEC staff comments have focused on areas that require significant judgment or involve estimates
  - Comments have often been resolved by providing the staff with a better understanding of the judgments made by management or by agreeing to provide additional disclosure in future filings
- The SEC staff encourages registrants to refine and supplement future disclosures, especially those that relate to significant judgments and estimates
  - ASC 606 requires disclosure of judgments made (and changes in those judgments) that significantly affect the determination of the amount and timing of revenue from contracts with customers

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Areas of frequent SEC staff comment (continued)
Management's discussion and analysis

- Results of operations
  - Discuss key metrics clearly and completely and how those metrics correlate with material changes in the results of operations
  - Disclose significant changes and why they occurred
    - Identify and quantify specific business drivers of results

Known trends and uncertainties	
Type of exposure:	**Describe effect of:**
Political conditions (e.g., changes in US trade agreements with other countries, trade tariffs)	Revenue reduction or increase in cost of raw materials
Foreign exchange fluctuations	Foreign currency gains and losses, results of foreign operations
Changes in interest rates	Liquidity and financing costs

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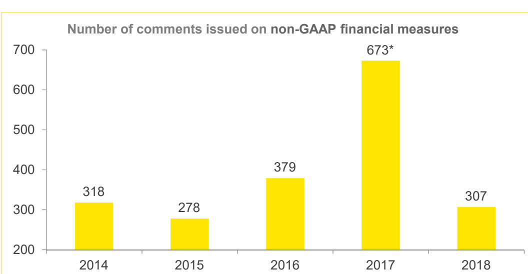
Areas of frequent SEC staff comment (continued)
Decline in comments on non-GAAP measures



* Updated Compliance and Disclosure Interpretations (C&DIs) issued in May 2016

Source: Audit Analytics – SEC UPLOAD comment letters on non-GAAP financial measures for the period from 1 July 2013 to 30 June 2018

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Areas of frequent SEC staff comment (continued)
Non-GAAP measures

- Prominence of non-GAAP measures
  - Omitting comparable GAAP measures
  - Volume and order of discussion
  - Omitting quantitative reconciliations for forward-looking non-GAAP measures
- Tailoring recognition and measurement principles
  - Accelerating the recognition of deferred revenue
  - Accounting for operating leases as capital leases
  - Eliminating the allowance for loan losses

We expect the SEC staff to question companies that present non-GAAP financial measures that unwind the effects of new accounting standards for purposes other than providing the required transition disclosures.

Areas of frequent SEC staff comment (continued)
Segment reporting

- Identification of the chief operating decision maker (CODM)
  - Registrants shouldn't default to the chief executive officer as the CODM
  - CODM does not need to have ultimate decision-making authority
- Identification of operating segments
  - Neither organizational structure nor reports provided to CODM are determinative
  - Emphasis should be on how the business is managed
- Aggregation of operating segments into reporting segments
  - Consider similar economic characteristics and all qualitative criteria
    - No bright lines on similar economic characteristics; future doesn't overcome past
  - Similarity viewed from the perspective of a reasonable investor
- Providing appropriate disclosures
  - Entity-wide disclosures
  - Non-GAAP financial measures

Areas of frequent SEC staff comment (continued)
Goodwill impairment issues and contingencies

- Goodwill impairment issues
  - Challenges the timing of goodwill impairment charges
  - Requests additional disclosures about reporting units that may be at risk of goodwill impairment
- Contingencies
  - Questions the failure to make required note disclosures when losses are considered reasonably possible or to disclose the range of reasonably possible losses
  - Requests that registrant use terms that are consistent with the language in ASC 450 when discussing the likelihood of occurrence (i.e., probable, reasonably possible or remote)

Areas of frequent SEC staff comment (continued)
Looking ahead

- Staff Accounting Bulletin (SAB) Topic 11.M (SAB 74) disclosures about potential effects of adoption should evolve as the effective date of a new standard approaches
  - Provide quantitative and qualitative information
  - Disclose expected quantitative effects on the financial statements; if they are unknown, disclose qualitative information to help the reader assess the potential significance of the effect on the registrant's financial statements
  - Describe the process being used to assess the effect of the new standards
- Accounting for income tax reform (SAB 118)
  - Disclosure should evolve over the course of the year
  - Application of the SAB should not be a deferral of accounting for tax reform – late adjustments could be challenged
- Cybersecurity
  - Avoid boilerplate cybersecurity risk and risk management governance disclosures
  - Timely disclose cyber risks and incidents that could have a material effect on a registrant

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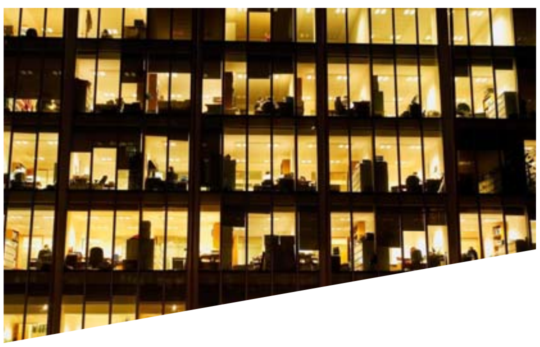
PCAOB update



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PCAOB overview

- Five new PCAOB members have joined
- PCAOB asked for public comment on its strategic plan for the first time
  - Plan will be finalized in November 2018
- Focus on audit quality continues
- Core values preliminarily identified:
  - Integrity
  - Excellence
  - Effectiveness
  - Collaboration
  - Accountability

"As an organization, we must and will be a trusted leader in driving continuous improvement in audit quality. We also must be proactive, responsive, and innovative in overseeing the audit profession."

— PCAOB Chairman William D. Duhnke

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Auditor's reporting model
Critical audit matters (CAMs) – timeline

Phase 1 effective (e.g., auditor tenure, form of report)

2017 | 2018 | 2019 | 2020

Management, audit committees and auditors should discuss:

- CAM reporting requirements
- Auditor's approach to implementing requirements
- Potential effect on auditor's report

CAMs effective for all other filers

CAMs effective for large accelerated filers for fiscal years ending on or after 30 June 2019

EY

Auditor's reporting model
CAMs

Critical audit matters

- Communicated or required to be communicated to the audit committee
- Related to accounts or disclosures that are material to financial statements
- Involved especially challenging, subjective or complex auditor judgment, considering:
  - Risks of material misstatement, including significant risks
  - Degree of auditor subjectivity and judgment
  - Nature and timing of significant unusual transactions
  - Nature and extent of audit effort and nature of evidence

- Audit report will identify the CAMs and include:
  - Principal considerations in making determinations
  - Description of how matters were addressed in the audit
  - Relevant financial statement accounts or disclosures

EY

Auditor's reporting model
CAMs – planning considerations

Early discussion of CAMs will help avoid surprises and allow time for resolving concerns

- Management and the audit committee should:
  - Understand the types of matters that may be CAMs
  - Review the draft description of the CAMs
  - Evaluate the effect on financial reporting processes
  - Understand the requirements of the standard and evaluate the effect on the audit process, including:
    - Determining whether additional internal parties should be involved in the review of the audit report
    - Understanding the auditor's timeline for implementation
    - Anticipating questions from investors, regulators and others
    - Assessing whether to change disclosures in areas related to CAMs

EY

PCAOB inspections: anticipated focus

- PCAOB inspections and activities will likely focus on:
  - Recurring areas of deficiencies, such as assessing and responding to risks of material misstatement
  - Review controls
  - Auditing accounting estimates, including fair value measurements
  - Economic risks
    - Business combinations
    - Effect of natural disasters on the insurance, banking and retail industries
    - Higher risk financial instruments
    - Trade protection
    - Regulatory policy environment
  - Implementation of new accounting standards, with a focus on the new revenue standard, including:
    - Audits of issuers that early adopted the revenue standard
    - How firms and audit teams prepared for the full implementation of the revenue standard

PCAOB inspections: anticipated focus (continued)

- Compliance with new requirements for the auditor's report
  - Information about auditor tenure, changes in report format, auditor's responsibility
  - Evaluation of firms' processes to prepare for the incorporation of CAMs

PCAOB – reminders
Auditing estimates (proposed auditing standard)

- Proposal would replace three auditing standards with a single standard for auditing estimates, including fair value measurements
- Additional focus would be placed on addressing management bias and maintaining professional skepticism
- Three approaches for auditing estimates would be retained:
  - Testing the company's process
  - Developing an independent expectation
  - Evaluating subsequent events
- An appendix addressing the use of pricing information from pricing services and brokers or dealers would be included
- New guidance would address the valuation of investments based on investee financial statements

PCAOB – reminders
Using the work of specialists (proposed auditing standard)

- Proposal would address the following topics:
  - Using the work of a company's specialist
  - Supervising the work of auditor-employed specialists
  - Using the work of an auditor-engaged specialist
- Proposal would retain current definition of a specialist
  - Income taxes and information technology would be outside the scope of the proposed guidance
- It would expand requirements for testing and evaluating the work of a company specialist
- It would largely align requirements for the auditor to supervise specialists, whether employed or engaged

PCAOB – reminders
Supervision of other auditors (proposed auditing standard)

- Proposal would strengthen the requirements for lead auditors to plan, supervise and evaluate the work of other auditors
- Proposal would introduce new terms:
  - Lead auditor
  - Other auditors
  - Referred-to auditors
- Supplemental request for comment was issued on the 2016 proposal

PCAOB – reminders
Going concern (agenda project)

- PCAOB is evaluating potential revisions to its standard on the auditor's going concern evaluation
  - Staff Audit Practice Alert No. 13 notes that in addition to considering the applicable financial reporting framework, auditors should continue to follow existing PCAOB auditing standards
- AICPA issued SAS No. 132 that was effective for audits of financial statements for periods ending on or after 15 December 2017
  - Statement changes the auditor's responsibilities
    - Requires an evaluation of management's assessment of going concern
    - Clarifies the responsibility to separately conclude on the appropriateness of the use of the going concern basis of accounting
    - Requires audit evidence about the intent and ability of a third party or owner-manager to provide financial support
    - Broadens communication requirements to those charged with governance

FASB update

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EY

FASB update

- Recently issued FASB standards
  - Recognition and measurement of financial assets and liabilities (ASU 2016-01)
  - Sale of nonfinancial assets (ASU 2017-05)
  - Statement of cash flows (ASU 2016-15)
  - Income taxes (ASU 2016-16)
  - Reclassification of certain tax effects from AOCI (ASU 2018-02)
  - Targeted improvements to accounting for hedging activities (ASU 2017-12)
  - Improvements to nonemployee share-based payment accounting (ASU 2018-07)
  - Credit Losses (ASU 2016-13)
  - Simplifying the test for goodwill impairment (ASU 2017-04)
  - Cloud computing – implementation costs (ASU 2018-15)
  - Disclosure framework
- FASB projects
  - Simplifying the balance sheet classification of debt
  - Improving the accounting for asset acquisitions and business combinations
  - Segment reporting
  - Financial performance reporting
  - Distinguishing liabilities from equity
  - Assumed liabilities in a revenue contract
- Restatement themes

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EY

Recently issued FASB standards

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EY

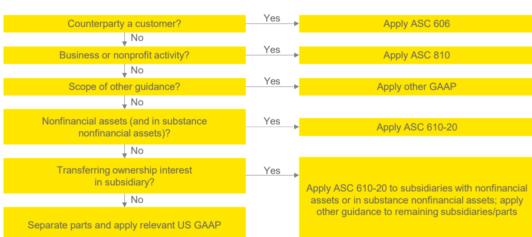
Recognition and measurement of financial assets and liabilities (ASU 2016-01)

- Targeted amendments to existing US GAAP include:
  - Equity investments are generally measured at fair value (FV) with changes in FV reported in net income (FV-NI)
  - A new measurement alternative is available for equity investments without readily determinable FVs
  - Changes in fair value caused by changes in instrument-specific credit risk (i.e., the entity's own credit risk) are recognized in other comprehensive income (OCI) for financial liabilities measured under the fair value option
  - Realizability of deferred tax assets (DTAs) related to available-for-sale (AFS) debt securities is assessed in combination with other DTAs
  - Fair value disclosures for financial instruments carried at amortized cost are reduced for public business entities (PBEs) and eliminated for non-PBEs

Effective dates of ASU 2016-01 for calendar year-end companies		
PBEs	Non-PBEs	Early adoption?
Q1 2018	2019	Non-PBEs: Q1 2018

EY

Sale of nonfinancial assets (ASU 2017-05)



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Sale of nonfinancial assets (continued) (ASU 2017-05)

- Derecognition
  - Step 1: Evaluate controlling financial interest (ASC 810)
  - Step 2: Determine whether control of asset transfers (ASC 606)
- Measurement
  - Consideration received is the transaction price determined in accordance with ASC 606 (including variable consideration)
  - Any non-controlling interest is measured at fair value
  - Seller recognizes a full gain or loss
- Adoption
  - Concurrent with ASC 606
  - Full or modified retrospective adoption (transition may be different than ASC 606

EY

Statement of cash flows (ASU 2016-15)
Classification of certain cash receipts and cash payments

- Clarifies how entities should classify certain cash receipts and cash payments on the statement of cash flows
- Also clarifies how the predominance principle should be applied when transactions have aspects of more than one class of cash flows
  - Early adoption is allowed, but all of the guidance must be adopted in the same period
  - The amendments will be applied retrospectively to all prior periods presented in the year of adoption
  - If it is impracticable to apply the amendments retrospectively for an issue, the amendments related to that issue would be applied prospectively

Effective date for calendar year end companies		
PBEs	Other entities	Early adoption
2018	2019	Yes

Statement of cash flows (ASU 2016-15)
Classification of certain cash receipts and cash payments

Topic	Classification
Debt prepayment or extinguishment costs	► Financing
Settlement of zero-coupon debt instruments or other debt instruments with coupon rates that are insignificant in relation to the effective interest rate of the borrowing: ► Portion attributable to interest ► Portion attributable to principal	 ► Operating ► Financing
Contingent consideration payments after a business combination: ► Made soon after ► Not made soon after: ► Up to fair value of acquisition date contingent consideration liability ► In excess of fair value of acquisition date contingent consideration liability	 ► Investing ► Financing ► Operating
Proceeds from settlement of insurance claims	► Nature of the loss
Proceeds from settlement of company-owned life insurance, including bank-owned life insurance: ► Settlement proceeds ► Premiums	 ► Investing ► Operating, investing or both
Distributions received from equity method investees:* ► Return on investment ► Return of investment * Entities are required to make a policy election to apply one of two approaches to determine when the cash distributions represent a return on investment rather than a return of investment.	 ► Operating ► Investing
Beneficial interests in securitization transactions: ► Interest retained ► Subsequent receipts	 ► Noncash disclosure ► Investing

Income taxes (ASU 2016-16)
Intra-entity asset transfers

Current GAAP	ASU 2016-16
Inventory	
Defer income tax effect on intercompany sales or transfers of assets until asset leaves consolidated group	No change
Non-inventory	
Defer income tax effect on intercompany sales or transfers of assets until asset leaves consolidated group	Recognize income tax effect in the period the intercompany sale or transfer occurs

Modified retrospective approach with a cumulative catch-up adjustment to opening retained earnings in the period of adoption

Effective date for calendar year-end companies		
PBEs	Other entities	Early adoption
2018	2019	Yes

Tax reform – reclassification of certain tax effects from AOCI (ASU 2018-02)

- Gives companies the option to reclassify to retained earnings the stranded tax effects from tax reform in accumulated other comprehensive income (AOCI)
  - Does not change the ASC 740 prohibition on backward tracing
- Provides a policy election to reclassify to retained earnings all tax effects related to items in AOCI stranded as a result of US tax reform even if they don't directly relate to the change in federal rate
  - Includes available-for-sale securities, pensions/employee benefit plans, foreign currency, hedging
- Includes new disclosure requirements for all entities, even if the option is not elected

Effective date for calendar year-ends		
All entities	Transition method	Early adoption?
Q1 2019	Retrospective or period of adoption	Yes

Targeted improvements to accounting for hedging activities (ASU 2017-12)

- FASB made targeted amendments to enable entities to better portray the economics of their risk management activities in the financial statements
  - Also simplifies certain aspects of hedge accounting
- Amendments are intended to:
  - Expand risks that are eligible to be hedged
  - Provide users with better insight into hedging strategies and their effectiveness
  - Reduce the complexity of applying hedge accounting
- Many aspects of ASC 815 remain unchanged
  - All guidance in ASC 815 not related to hedge accounting
  - "Highly effective" threshold

Effective dates for calendar-year entities			
Transition method	Public business entities (PBEs)	Non-PBEs	Early adoption?
Generally modified retrospective	Q1 2019	2020	Yes

Improvements to nonemployee share-based payment accounting (ASU 2018-07)

Applies to instruments issued to nonemployees in exchange for goods and services, not for raising capital or selling goods and services

	Before ASU 2018-07	After ASU 2018-07	ASC 718
Measurement date for equity-classified awards	Earlier of: ► Performance commitment date ► Performance completion date	Generally grant date	
Term	Contractual term	Expected term or contractual term	Expected term
Post-vesting classification	Reassessed when performance is complete	Reassessed if modified after grantee is no longer providing goods or services	

Improvements to nonemployee share-based payment accounting (ASU 2018-07) (continued)

- Allows nonpublic entities to use two practical expedients for nonemployee awards that are already available for employee awards
  - The same accounting policies must be used for awards to both employees and nonemployees
- Applies to equity-classified awards that don't have a measurement date and unsettled liability-classified awards
  - Recognize a cumulative-effect adjustment to retained earnings at beginning of the annual period of adoption
  - Remeasure incomplete assets that include nonemployee share-based payment costs (e.g., work-in-process inventory, construction-in-progress)

Effective for calendar year-end entities		
Public business entities (PBEs)	Non-PBEs	Early adoption?
2019	2020	Permitted if ASC 606 has been adopted

Credit losses (ASU 2016-13)
Overview

All entities

Current expected credit loss (CECL) model
- Financial assets measured at amortized cost:
  - Trade receivables, reinsurance receivables, loans, held-to-maturity (HTM) debt securities, reverse repos
- Net investment in leases recognized by a lessor
- Off-balance-sheet credit exposures not accounted for as insurance

AFS debt security impairment model
- Available-for-sale (AFS) debt securities

Model for certain beneficial interests classified as HTM or AFS that are not of high credit quality

Core concepts of the CECL model
Based on amortized cost
Considers the risk of loss, even if remote
Reflects losses over an asset's contractual life
Considers past events, current conditions and expectations of the future

- The objective of the CECL model is to recognize an allowance for credit losses that results in the financial statements reflecting the net amount expected to be collected
- The CECL model requires a recognition of credit loss on almost all in-scope assets at origination and will require new disclosures
- The CECL model is expected to result in increased earnings volatility and will involve more judgment
- ASU 2016-13 also makes targeted changes to the accounting for AFS debt securities, replacing today's concept of other-than-temporary impairment (OTTI)

Credit losses (ASU 2016-13)
Effective date and transition

Effective date for calendar year-end companies			
Public business entities (PBEs) that are SEC filers	Other PBEs	All other entities*	Early adoption?
2020	2021	2021	Yes, but no earlier than 2019

* The FASB proposed changing the effective date for non-PBEs to in 2022

- An entity will apply the new guidance using a modified retrospective approach and recognize a cumulative-effect adjustment as of the beginning of the first reporting period in which the guidance is effective
- Implementation efforts should be underway – entities will likely need to gather and retain additional data and enhance modeling capabilities and processes and controls

Simplifying the test for goodwill impairment (ASU 2017-04)

	Current GAAP	ASU 2017-04
Step 1	Determine whether fair value of reporting unit is less than its carrying amount	
Step 2	Determine the implied fair value of goodwill (reporting unit's fair value less fair value of assets and liabilities)	N/A
Impairment	Excess of carrying amount of goodwill over its implied fair value	Excess of carrying amount of reporting unit over its fair value

Effective dates for calendar year-end companies		
SEC filers	Other PBEs	Non-PBEs
2020	2021	2022

- Applied prospectively
- Early adoption is permitted

Simplifying the test for goodwill impairment (ASU 2017-04) (continued)

Example	
Fair value of reporting unit	92
Carrying amount of reporting unit	100
Fair value of identified assets and liabilities	80
Carrying amount of goodwill	15

	Current GAAP	ASU 2017-04
Step 1	Fair value of reporting unit (92) is less than carrying amount of reporting unit (100)	
Step 2	Implied fair value of goodwill: 12 (92–80)	N/A
Impairment	3 (15–12)	8 (100–92)

Cloud computing – implementation costs (ASU 2018-15)

- A customer in a cloud computing arrangement (i.e., hosting arrangement) that is a service contract will follow the internal use software guidance in ASC 350-40 to determine which implementation costs to defer and recognize as an asset
- Certain implementation costs incurred will be deferred and recognized as an asset
  - Expense over the term of the hosting arrangement
  - Classify expense in the same income statement line item as the hosting arrangement fees
- Customers will follow existing US GAAP to account for other implementation costs
- New guidance does not affect the accounting for the hosting arrangement component of a contract

Effective dates for calendar year-end entities		
PBEs	Non-PBEs	Early adoption?
2020	2021	Yes

Disclosure framework

- The FASB made changes to its Conceptual Framework and issued two ASUs as part of its project to improve the effectiveness of disclosures
- A new chapter in the Conceptual Framework provides a framework for the Board to use when evaluating new and existing disclosure requirements
  - The new chapter also discusses considerations for the Board to use in evaluating interim disclosures
- The FASB reinstated the definition of materiality that was used in FASB Concepts Statement No. 2
  - The definition of materiality is consistent with other definitions of materiality in the financial reporting system

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Disclosure framework (continued)

- Topic-specific disclosure reviews
  - Final standards were issued on disclosures related to fair value measurement (ASU 2018-13) and defined benefit plans (ASU 2018-14)
  - Income taxes: FASB is redeliberating exposure draft
  - Inventory: FASB is conducting additional outreach in response to comments received on exposure draft
- Evaluation of interim reporting requirements – more research needed

Effective date for calendar year-end companies			
ASU 2018-13	ASU 2018-14		
All entities	PBEs	Other entities	Early adoption?
2020	2021	2022	Yes

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FASB projects

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Simplifying the balance sheet classification of debt

- Proposal would replace today's rules-based guidance with a principle for classifying debt as current or noncurrent
  - Would apply to all "debt arrangements," as well as convertible debt, lease liabilities (ASC 842) and mandatorily redeemable financial instruments (ASC 480)
- Debt would be classified as noncurrent if either:
  - Liability is contractually due to be settled more than one year (or operating cycle, if longer) after the balance sheet date
  - Entity has a contractual right to defer settlement of the liability for at least one year (or operating cycle, if longer) after the balance sheet date
- Emphasis would be on legal rights that exist as of reporting date
  - Exception for waivers of debt covenant violations, provided certain conditions are met
- Final standard is expected in the 1st quarter of 2019

Other proposals and projects

- Improving the accounting for asset acquisitions and business combinations
  - Project to consider whether certain areas in the accounting for asset acquisitions and business combinations can be aligned
- Segment reporting – aggregation and disclosures
  - Project intends to improve the aggregation criteria and segment disclosures
  - FASB staff is performing extended outreach
- Financial performance reporting – disaggregation of performance information
  - Project aims to improve the decision-usefulness of the income statement through the disaggregation of performance information
    - Project is currently focused on the disaggregation of lines that represent the cost of revenue and selling, general and administrative expenses

Other proposals and projects (continued)

- Distinguishing liabilities from equity (including convertible debt)
  - Project to reduce complexity of accounting for financial instruments with characteristics of liabilities and equity
    - Focus on guidance on indexation and settlement (ASC 815-40), convertible instruments (ASC 470-20), disclosures and earnings per share
  - FASB discussed direction of the project in June 2018

Other proposals and projects (continued)

- Recognition under Topic 805 for an assumed liability in a revenue contract (EITF Issue 18-A)
  - Acquiring entities in business combinations would apply the definition of a performance obligation in ASC 606 to determine whether to recognize an assumed liability for an acquired contract with a customer
    - The assumed liability would be measured at fair value
  - Entities historically applied the concept of a legal performance obligation in determining whether to recognize deferred revenue for an acquired revenue contract
    - A performance obligation, as defined in ASC 606, does not need to be legally enforceable
  - The effective date will be determined at a future EITF meeting

Restatement themes

Restatement themes
Overview

Top three topics – 2017	%	Top three topics – 2016	%
Income taxes	13	Income taxes	16
Revenue recognition	12	Revenue recognition	9
Reclassifications (balance sheet), accrued liabilities and goodwill/intangible assets	6 each	Reclassifications (balance sheet and income statement)	6 each

- Practices that may lessen the likelihood of errors/restatements include:
  - Identifying and accounting for key contractual terms
  - Focusing on changes in business and effects on estimates on a timely basis
- Entities should correct identified errors as soon as practicable to avoid restatement due to an accumulation of individually immaterial errors