

PRIVATE COMPANY ACCOUNTING UPDATE






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TODAY'S AGENDA

-  **COVID Update**
-  **Major FASB Projects Update**
-  **Other Recent FASB Guidance**



COVID UPDATE

- Impact on Your Financial Statements
- Impact on the Audit or Review
- PPP Loans

COVID IMPACTING MANY AREAS OF BUSINESSES



Impact varies depending on industry and markets

Supply chain problems

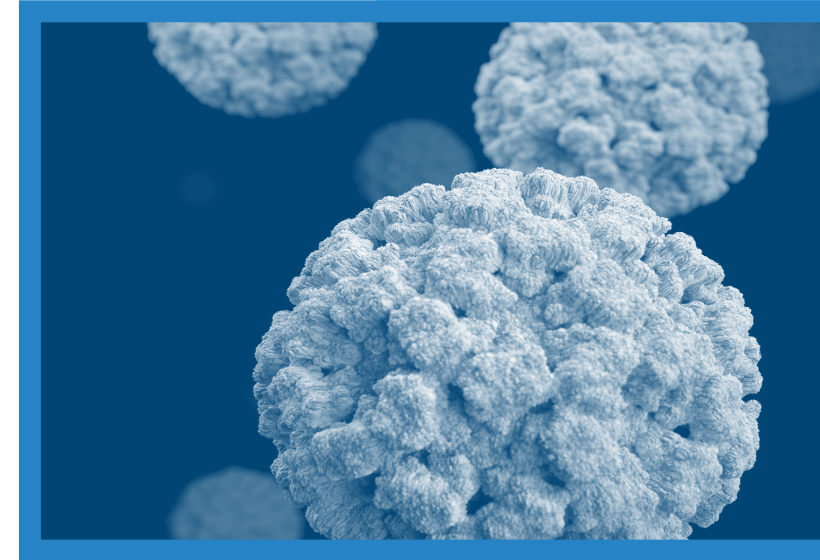
Major backlogs

Absenteeism, recruiting issues

Companies monitoring customer credit - no significant issues to date

For many rebounds in orders in second quarter with some return to profitability

Concerns on duration of recovery



IMPACT ON FINANCIAL STATEMENTS



Significant impact on 2020 estimates and disclosures

In 2019 was only a subsequent event. In 2020, significantly more impactful to amounts and disclosures

Best practice - disclosures tailored to how impacting company

- Boiler plate of little use

Consider ASC 275 – Risks and Uncertainty Disclosures

- Nature of operations and markets
- Significant estimates

Potential impact is pervasive:

- Liquidity, capital resources
- Operational challenges
- Impact on debt, covenants, debt service
- Capital expenditures
- Changes in customers, credit terms (required by revenue recognition guidance ASC 606)
- Federal assistance
- Going concern



IMPACT ON FINANCIAL STATEMENTS, CONT.



Receivables – allowances for doubtful accounts

Obsolescence and other inventory reserves

Self-insurance accruals especially health care

Carrying value of investments

Impairment of intangibles and goodwill

Property and equipment

Financial health of tenants

Right of use assets



FINANCIAL STATEMENTS - OTHER CONSIDERATIONS



Impact of lease concessions

Debt

Customer concessions - ASC 606, revenue recognition disclosures will require updating

If not meeting covenants, start process with lenders early and consider disclosures

Proceeds business interruption insurance (court decisions so far favoring insurers)

Exit and disposal cost obligation and activities



IMPACT ON THE AUDIT OR REVIEW



Control environment

Logistics

**More remote transactions and
remote access**

Physical controls updated



PAYCHECK PROTECTION PROGRAM (PPP)



Coronavirus Aid, Relief and Economic Security (CARES) Act created PPP loans in March 2020

- Provided incentive for small businesses to keep workers
- Through existing SBA 7(a) lender
- Period either 2 or 5 years, depending if issued before or after June 5
- Interest rate 1%
- No collateral/guarantees or fees
- Borrowers required to assess their economic need at time of application
- Generally, SBA will forgive loans if employee retention criteria met and funds used for eligible expenses



PAYCHECK PROTECTION PROGRAM (PPP), CONT.



Stopped accepting applications August 8

Funded 5.2 million loans - \$525 billion

Majority of loans < \$150K

SBA reserves the right to review any loan

SBA will review loans over \$2 million



PPP FORGIVENESS



Borrowers can apply for forgiveness

Loans <\$50k only submit Form 3508S

- Ignores reductions in FTEs or wage rates

Forgiveness based on eligible expenses in either an 8 or 24 week period (covered period)

Borrower repayments begin 10 months after covered period ends

End of September 2020, 96,000 forgiveness applications received – none yet approved



ACCOUNTING FOR PPP LOANS



AICPA provided guidance on accounting for PPP loans

Legal form is debt but substance can be seen as government grant

No U.S. guidance for businesses receiving government grants – AICPA pointed to IAS 20

If meet threshold that forgiveness reasonably assured, accounting policy election to follow U.S. GAAP debt and interest rules or IAS 20

If debt:

- Accrue interest as incurred
- Remains a liability until legally forgiven
- Record a gain when forgiven



ACCOUNTING FOR PPP LOANS, CONT.



If follow government grant accounting:

- Record PPP loan as a deferred income liability
- Take to income statement on a systematic basis over period of related costs
- Use separate line like “other income” or net against the related expenses

Disclosures will be significant:

- Explain policy election
- Normal debt disclosures – interest rate, repayment terms
- If take to income statement, disclose amounts and in which captions included
- Discussion on amount expected to be forgiven
- Contingent liability for repayment





MAJOR FASB PROJECTS UPDATE

- Revenue Recognition
- Leases
- Financial Instruments – Credit Losses

ASU 2020-05 – REVENUE RECOGNITION AND LEASES



Revenue from Contracts with Customers (Topic 606) and Leases (Topic 842) - Effective Dates for Certain Entities

A response to COVID 19

Revenue recognition deferred for one year

- Nonpublic entities that have not yet issued financial statements (or made financial statements available for issuance)
- May elect to adopt for annual periods beginning after December 15, 2019
- Early adoption permitted

Leases - private entities may defer to fiscal years beginning after December 15, 2021

- Early adoption permitted





Lessons Learned From Adoption Of Revenue From Contracts with Customers (Topic 606)

- Some industries were impacted significantly:
 - Franchisors
 - Gift cards
 - Construction
 - Technology and software
- Otherwise, similar to public companies, few restatements
- Issues with complex or unusual transactions including over-time revenues
- Some exporters impacted - in some countries or under contracts ownership may only pass when product enters foreign country
- Changes in disclosures were significant



ASU 2016-02 - LEASES (TOPIC 842)



ASC Topic 842, Leases, issued February 2016 via ASU 2016-02

- Almost 10 years in the making
- Will replace legacy ASC Topic 840

Lessees will recognize almost every lease on the balance sheet but very little has changed for lessors

Retains concept of operating versus finance (capital) leases for income statement and cash flow statement and decision of operating versus finance is largely unchanged

Starting point for ROU asset is not always the same as ROU liability

Date Change

- Calendar year-end nonpublic entities first required to adopt in December 31, 2022 financials
- Transition method options
- Practical expedients



LEASES (TOPIC 842) – IMPLEMENTATION ISSUES



What is a lease?

- Short-term or month-to-month leases

US GAAP / IFRS practical considerations

- No separation of operating and finance for IFRS
- Low value/immaterial leases

Related party leases

Renewal options

Leases indexed to CPI

What have we learned?





Measurement of credit losses on financial instruments

- Introduces the current expected credit losses model (CECL)
- Replaces the incurred loss model – losses recognized earlier
- More judgment and assumptions
- Increased disclosures
- Nonpublic entities – first effective for calendar year 2021
- Early adoption permitted
- Apply using modified retrospective approach
- Targeted Transition Relief (ASU 2019-05) and Codification Improvements (ASU 2019-11)





OTHER RECENT FASB GUIDANCE





Simplifying the test for goodwill impairment

- Applies to entities that have not adopted private company alternative for goodwill - based on a triggering event
- Option to first perform qualitative assessment to determine if qualitative test is necessary
- Eliminates step 2 from the goodwill impairment test to reduce cost and complexity of evaluation
- Applied prospectively
- Nonpublic entities – first effective calendar year 2022
- Early adoption permitted





Presentation and disclosures by not-for-profit entities for contributed nonfinancial assets

- Objective to increase transparency of contributed nonfinancial assets
- A separate line on statement of activities
- Expanded disclosures
- Applied retrospectively
- Effective for annual periods beginning after June 15, 2021
- Early adoption permitted



ASU 2018-15 - INTANGIBLES - GOODWILL AND OTHER – INTERNAL USE SOFTWARE (SUBTOPIC 350-40)



Customer's accounting for implementation costs incurred in a cloud computing arrangement that is a service contract

- Clarifies requirements for capitalizing implementation costs
- License for internal-use software
- Presentation considerations
- Nonpublic entities – first effective calendar 2021
- Early adoption permitted





Inclusion of the Secured overnight financing rate (SOFR) overnight index swap (OIS) rate as a benchmark interest rate for hedge accounting purposes

- Introduced due to phase-out of the London Interbank Offered Rate (LIBOR) swap rate by end of 2021
- OIS rate based on SOFR now eligible
- Other eligible benchmark rates are as follows:
 - Interest rates on direct treasury obligations of the U.S. Government (UST)
 - LIBOR
 - OIS Rate based on the Fed Funds Effective Rate
 - Securities Industry and Financial Markets Association (SIFMA) Municipal Swap Rate – introduced as part of ASU 2017-12
- Effective calendar 2020 on a prospective basis





Facilitation of the effects of reference rate reform on financial reporting

- Temporary optional expedients and exceptions for contract modifications and hedging accounting if certain criteria are met
- Effective through December 31, 2022
- Intended to ease the potential burden in accounting for reference rate reform on financial





Targeted improvements to related party guidance for variable interest entities

- Supersedes private company alternative for common control leasing arrangements
- Parent Co and entity being evaluated cannot be public entities
- May elect to not apply VIE guidance to entities under common control
- Policy election applies to all existing and future common control arrangements
- Detailed disclosures regarding exposure still required
- Expanded guidance on whether fees payable to decision makers and service providers are variable interests
- Nonpublic entities – first effective calendar 2021
- Early adoption permitted



ASU 2019-12 - INCOME TAXES (TOPIC 740)



Simplifying Income Taxes

- Removes the following exceptions:
 - Incremental approach for intraperiod tax allocation when there is a loss from continuing operations and income or a gain from other items
 - Requirement to recognize a deferred tax liability (DTL) for equity method investment in foreign subsidiaries
 - The ability not to recognize a DTL for a foreign subsidiary when a foreign equity method investment becomes a subsidiary
 - The general methodology for calculating income taxes in an interim period when a year-to-date loss exceeds the anticipated loss for the year
- Requires franchise or similar tax partially based on income to be recognized as an income-based tax and any incremental amount as a non-income-based tax.





Simplifying Income Taxes

- Requires an entity to evaluate when a step up in tax basis of goodwill should be considered part of the business combination instead of a separate transaction
- Specifies that an entity is not required to allocate the consolidated amount of current and deferred tax expense to a legal entity that is not subject to tax. However, an entity may elect to do so for an entity that is both not subject to tax and disregarded by the taxing authority
- Requires an entity to reflect the effect of an enacted change in tax law or rates in the interim period of the enactment
- Nonpublic entities – first effective calendar 2022
- Early adoption is permitted





THANK YOU



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