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Banking & Securities

Accounting and Financial Reporting Update

November 4, 2016

Contents

Foreword iv

Acknowledgments and Contact Information v

Introduction vi

Updates to Guidance 1

Financial Instruments 2

Impairment 2

Classification and Measurement 9

Recognition of Breakage for Prepaid Stored-Value Products 11

Effect of Derivative Contract Novations on Existing Hedge Accounting 12

Contingent Put/Call Options in Debt Instruments 14

Leases 15

Revenue Recognition 18

Simplifying the Transition to the Equity Method of Accounting 25

Consolidation — Interests Held Through Related Parties That Are Under Common Control 26

Employee Share-Based Payment Accounting Improvements 28

Classification of Deferred Taxes 32

Accounting for Income Taxes: Intra-Entity Asset Transfers 34

Statement of Cash Flows: Classification of Certain Cash Receipts and Cash Payments 36

Alternatives for Private Companies 40

On the Horizon 41

Financial Instruments 42

Hedging 42

Liabilities and Equity — Targeted Improvements 45

Accounting for Interest Income Associated With the Purchase of Callable Debt Securities 47

Simplifying the Balance Sheet Classification of Debt 48

Goodwill and Business Combinations 50

Subsequent Accounting for Goodwill for Public Business Entities and Not-for-Profit Entities, Including Goodwill Impairment 50

Clarifying the Definition of a Business 51

Accounting for Identifiable Intangible Assets in a Business Combination 53

Accounting for Partial Sales of Nonfinancial Assets 53

Stock-Based Compensation and Employee Benefits 54
Nonemployee Share-Based Payment Accounting Improvements 54
Employee Benefit Plan Master Trust Reporting (EITF 16-B) 55
Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost 56
Restricted Cash 57
Disclosures by Business Entities About Government Assistance 58
Disclosure Framework 59
FASB's Decision Process 59
Entity's Decision Process 60
Topic-Specific Disclosure Reviews 60
Fair Value Measurement 60
Income Taxes 63
Defined Benefit Plans 66

Other Topics 67

Banking and Securities Regulatory Updates 68
SEC and AICPA Updates 68
Summary of Accounting Pronouncements Effective in 2016 79

Appendixes 83

Appendix A — Glossary of Standards and Other Literature 84
Appendix B — Abbreviations 92
Appendix C — Other Resources 94

Foreword

November 4, 2016

To our clients and colleagues in the banking and securities sector:

We are pleased to announce our ninth annual accounting and financial reporting update. The topics discussed in this publication were selected because they may be of particular interest to banking and securities entities.

Some of the notable standard-setting developments in 2016 were (1) the issuance of new guidance on measurement of credit losses on financial instruments, (2) the issuance of new guidance on classification and measurement of financial instruments, (3) the issuance of new guidance on accounting for leases, (4) the issuance of refinements to the new guidance on recognition of revenue from contracts with customers, and (5) the SEC's continued focus on rulemaking, particularly in connection with its efforts to complete mandated actions under the Dodd-Frank Act.

This publication is divided into three sections: (1) "Updates to Guidance," which highlights changes to accounting and reporting standards that banking and securities entities need to start preparing for now; (2) "On the Horizon," which discusses standard-setting topics that will affect banks and other financial institutions as they plan for the future; and (3) "Other Topics" that may be of interest to entities in the banking and securities sector. This year's Other Topics section also contains a table that lists accounting pronouncements that became effective in 2016.

The 2016 accounting and financial reporting updates for the insurance, investment management, and real estate sectors are available (or will be available soon) on US GAAP Plus, Deloitte's Web site for accounting and financial reporting news.

As always, we encourage you to contact your local Deloitte office for additional information and assistance.

Sincerely,

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Introduction

The year 2016 has seen continued economic improvement, as evidenced by increasing consumer confidence, strong market performance, and the Federal Reserve's continued focus on raising the federal funds rate. Increased profitability has continued as a result of lower loan-loss provisions and a focus on cutting costs throughout all aspects of banking and securities institutions; however, expenses associated with complying with new regulations will continue to put downward pressure on earnings.

Economic Environment

The banking and securities industry continues to be affected by costs and complexities of litigation as well as increasing domestic and global regulatory requirements. Residential, commercial, and consumer lending have continued to grow, and allowances for loan-loss provisions have dropped and remain at pre-crisis levels. However, institutions with high concentrations of credits in certain industries, especially the oil and gas industry, have faced and may continue to face increased allowances for loan losses because of the significant challenges in these industries — specifically, the significant decrease in oil and gas prices since the fourth quarter of 2015.

Financial Reporting Developments

New Revenue Recognition Standard

In 2014, the FASB[1] and IASB issued new guidance on the recognition of revenue from contracts with customers (ASU 2014-09[2] and IFRS 15, respectively). The FASB continued to refine this guidance throughout 2015 and 2016. In response to requests from stakeholders, as well as continued feedback from primary financial statement users and preparers, the FASB issued ASU 2015-14, which defers implementation of the revenue standard by one year for all entities and permits early adoption on a limited basis. For public business entities (as well as not-for-profit entities and conduit bond obligors), the standard is effective for annual reporting periods beginning after December 15, 2017. For nonpublic entities, the standard is effective for annual reporting periods beginning after December 15, 2018.

In 2016, the FASB issued a number of ASUs that refine the guidance in the new revenue standard, including ASU 2016-08, which addresses certain principal-versus-agent considerations specific to reporting revenue gross versus net. The transition resource group (TRG) for revenue recognition will continue to discuss activities related to banking and securities institutions' implementation of the new revenue standard.

[1] For a list of abbreviations used in this publication, see Appendix B.
[2] For the full titles of standards, topics, and regulations used in this publication, see Appendix A.

New Guidance on Measurement of Credit Losses on Financial Instruments

After several years of deliberations and exposure drafts, the FASB issued ASU 2016-13 on measurement of credit losses on financial instruments. The ASU introduces the current expected credit loss (CECL) model to U.S. GAAP. This CECL model will require entities to record all losses that are expected for the life of the financial instrument. The ASU does not provide specific methods for measuring the expected credit losses; rather, the principles-based guidance allows individual institutions to develop their own calculations to reflect their expected credit losses, and it permits certain practical expedients. In addition, the ASU makes certain improvements to the existing other-than-temporary impairment model in ASC 320 for certain available-for-sale (AFS) debt securities to eliminate the concept of "other than temporary" from that model.[3]

For public business entities that meet the U.S. GAAP definition of an SEC filer, the ASU is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. For public business entities that do not meet the U.S. GAAP definition of an SEC filer, the ASU is effective for fiscal years beginning after December 15, 2020, including interim periods within those fiscal years. For all other entities, the ASU is effective for fiscal years beginning after December 15, 2020, and interim periods within fiscal years beginning after December 15, 2021. Early adoption is permitted for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years.

Simplification Initiative

The FASB continues to work diligently toward improving existing accounting guidance under its simplification initiative (i.e., the Board's effort to reduce the cost and complexity of current U.S. GAAP while maintaining and enhancing the usefulness of the related financial statement information). The FASB issued guidance in 2016 on simplifying the transition to equity method accounting as part of ASU 2016-07 and is in various stages of deliberations and drafting exposure drafts on a variety of other simplification projects.

Additional Information

For additional information about industry issues and trends, see Deloitte's 2016 Financial Services Industry Outlooks.

[3] The amendments do not apply to an AFS debt security that an entity intends to sell or will more likely than not be required to sell before the recovery of its amortized cost basis. If an entity intends to sell or will more likely than not be required to sell a security before recovery of its amortized cost basis, the entity would write down the debt security's amortized cost to the debt security's fair value as required under existing U.S. GAAP.

Updates to Guidance

Financial Instruments

Impairment

Background

In June 2016, the FASB issued ASU 2016-13, which amends guidance on the impairment of financial instruments. The ASU adds to U.S. GAAP an impairment model (known as the current expected credit loss (CECL) model) that is based on expected losses rather than incurred losses. Under the new guidance, an entity recognizes as an allowance its estimate of expected credit losses, which the FASB believes will result in more timely recognition of such losses. The ASU is also intended to reduce the complexity of U.S. GAAP by decreasing the number of credit impairment models that entities use to account for debt instruments.

Once effective (see the "Effective Date" discussion below), the new guidance will significantly change the accounting for credit impairment. Banks and certain asset portfolios (e.g., loans, leases, and debt securities) will need to modify their current processes for establishing an allowance for loan and lease losses and other-than-temporary impairments to ensure that they comply with the ASU's new requirements. To do so, they may need to make changes to their operations and systems associated with credit modeling, regulatory compliance, and technology.

See Deloitte's June 17, 2016, *Heads Up* for additional information about ASU 2016-13.

Thinking It Through

In late 2015, the FASB established a transition resource group (TRG) for credit losses. Like the TRG for the new revenue recognition standard, the credit losses TRG does not issue guidance but provides feedback to the FASB on potential implementation issues. By analyzing and discussing such issues, the TRG helps the Board determine whether it needs to take further action (e.g., by clarifying or issuing additional guidance).

The CECL Model

Scope

The CECL model applies to most[1] debt instruments (other than those measured at fair value), trade receivables, lease receivables, reinsurance receivables that result from insurance transactions, financial guarantee contracts,[2] and loan commitments. However, available-for-sale (AFS) debt securities are excluded from the model's scope and will continue to be assessed for impairment under the guidance in ASC 320 (the FASB moved the impairment model for AFS debt securities from ASC 320 to ASC 326-30 and has made limited amendments to the impairment model for AFS debt securities, as discussed below).

[1] The following debt instruments would not be accounted for under the CECL model:
- Loans made to participants by defined contribution employee benefit plans.
- Policy loan receivables of an insurance entity.
- Pledge receivables (promises to give) of a not-for-profit entity.
- Loans and receivables between entities under common control.

[2] The CECL model does not apply to financial guarantee contracts that are accounted for as insurance or measured at fair value through net income.

Recognition of Expected Credit Losses

Unlike the incurred loss models in existing U.S. GAAP, the CECL model does not specify a threshold for the recognition of an impairment allowance. Rather, an entity will recognize its estimate of expected credit losses for financial assets as of the end of the reporting period. Credit impairment will be recognized as an allowance — or contra-asset — rather than as a direct write-down of the amortized cost basis of a financial asset. However, the carrying amount of a financial asset that is deemed uncollectible will be written off in a manner consistent with existing U.S. GAAP.

Thinking It Through

Because the CECL model does not have a minimum threshold for recognition of impairment losses, entities will need to measure expected credit losses on assets that have a low risk of loss (e.g., investment-grade held-to-maturity (HTM) debt securities). However, the ASU states that "an entity is not required to measure expected credit losses on a financial asset . . . in which historical credit loss information adjusted for current conditions and reasonable and supportable forecasts results in an expectation that nonpayment of the [financial asset's] amortized cost basis is zero." U.S. Treasury securities and certain highly rated debt securities may be assets the FASB contemplated when it decided to allow an entity to recognize zero credit losses on an asset, but the ASU does not so indicate. Regardless, there are likely to be challenges associated with measuring expected credit losses on financial assets whose risk of loss is low.

Measurement of Expected Credit Losses

The ASU describes the impairment allowance as a "valuation account that is deducted from the amortized cost basis of the financial asset(s) to present the net carrying value at the amount expected to be collected on the financial asset." An entity can use a number of measurement approaches to determine the impairment allowance. Some approaches project future principal and interest cash flows (i.e., a discounted cash flow method) while others project only future principal losses. Regardless of the measurement method used, an entity's estimate of expected credit losses should reflect those losses occurring over the contractual life of the financial asset.

When determining the contractual life of a financial asset, an entity is required to consider expected prepayments either as a separate input in the determination or as an amount embedded in the credit loss experience that it uses to estimate expected credit losses. The entity is not allowed to consider expected extensions of the contractual life unless it reasonably expects to execute a troubled debt restructuring with the borrower by the reporting date.

An entity must consider all available relevant information when estimating expected credit losses, including details about past events, current conditions, and reasonable and supportable forecasts and their implications for expected credit losses. That is, while the entity is able to use historical charge-off rates as a starting point for determining expected credit losses, it has to evaluate how conditions that existed during the historical charge-off period may differ from its current expectations and accordingly revise its estimate of expected credit losses. However, the entity is not required to forecast conditions over the contractual life of the asset. Rather, for the period beyond which the entity can make reasonable and supportable forecasts, the entity reverts to historical credit loss experience.

Thinking It Through

It will most likely be challenging for entities, particularly financial institutions, to measure expected credit losses. Further, one-time or recurring costs may be associated with the measurement, some of which may be related to system changes and data collection. While such costs will vary by institution, nearly all entities will incur some costs when using forward-looking information to estimate expected credit losses over the contractual life of an asset.

Unit of Account

The CECL model does not prescribe a unit of account (e.g., an individual asset or a group of financial assets) in the measurement of expected credit losses. However, an entity is required to evaluate financial assets within the scope of the model on a collective (i.e., pool) basis when assets share similar risk characteristics. If a financial asset's risk characteristics are not similar to the risk characteristics of any of the entity's other financial assets, the entity would evaluate the financial asset individually. If the financial asset is individually evaluated for expected credit losses, the entity would not be allowed to ignore available external information such as credit ratings and other credit loss statistics.

Thinking It Through

The ASU requires an entity to collectively measure expected credit losses on financial assets that share similar risk characteristics (including HTM securities). While certain loans are pooled or evaluated collectively under current U.S. GAAP, entities may need to refine their data-capturing processes to comply with the new requirements.

Practical Expedients for Measuring Expected Credit Losses

The ASU permits entities to use practical expedients to measure expected credit losses for the following two types of financial assets:

- *Collateral-dependent financial assets*[3] — In a manner consistent with the requirements under existing U.S. GAAP, the ASU permits an entity to measure its estimate of expected credit losses for collateral-dependent financial assets as the difference between the financial asset's amortized cost and the collateral's fair value (adjusted for selling costs, when applicable).
- *Financial assets for which the borrower must continually adjust the amount of securing collateral (e.g., certain repurchase agreements and securities lending arrangements)* — An entity is permitted to measure its estimate of expected credit losses on these financial assets as the difference between the amortized cost basis of the asset and the collateral's fair value.

Write-Offs

Like current guidance, the ASU requires an entity to write off the carrying amount of a financial asset when the asset is deemed uncollectible. However, unlike current requirements, the ASU's write-off guidance also applies to AFS debt securities.

AFS Debt Securities

The CECL model does not apply to AFS debt securities. Instead, the FASB decided to make targeted improvements to the existing other-than-temporary impairment model in ASC 320 for certain AFS debt

[3] The ASU defines a collateral-dependent financial asset as a "financial asset for which the repayment is expected to be provided substantially through the operation or sale of the collateral when the borrower is experiencing financial difficulty based on the entity's assessment as of the reporting date." Under the definition in current U.S. GAAP, an entity is not required to assess the borrower's financial wherewithal when determining whether the financial asset is collateral-dependent.

securities to eliminate the concept of "other than temporary" from that model.[4] Accordingly, the ASU states that an entity:

- Must use an allowance approach (vs. permanently writing down the security's cost basis).
- Must limit the allowance to the amount at which the security's fair value is less than its amortized cost basis.
- May not consider the length of time fair value has been less than amortized cost.
- May not consider recoveries in fair value after the balance sheet date when assessing whether a credit loss exists.

Thinking It Through

The Board did not revise (1) step 1 of the existing other-than-temporary impairment model (i.e., an "investment is impaired if the fair value of the investment is less than its cost") or (2) the requirement under ASC 320 for an entity to recognize in net income the impairment amount only related to credit and to recognize in other comprehensive income (OCI) the noncredit impairment amount. However, the ASU does require an entity to use an allowance approach for certain AFS debt securities when recognizing credit losses (as opposed to a permanent write-down of the AFS security's cost basis). As a result, the entity would reverse credit losses through current-period earnings on an AFS debt security in both of the following circumstances:

- If the fair value of the debt security exceeds its amortized cost in a period after a credit loss had been recognized through earnings (because fair value was less than amortized cost), the entity would reverse the entire credit loss previously recognized and recognize a corresponding adjustment to its allowance for credit losses.
- If the fair value of the debt security does not exceed its amortized cost in a period after a credit loss had been recognized through earnings (because fair value was less than amortized cost) but the credit quality of the debt security improves in the current period, the entity would reverse the credit loss previously recognized only in an amount that would reflect the improved credit quality of the debt security.

PCD Assets

For purchased financial assets with credit deterioration (PCD assets),[5] the ASU requires an entity's method for measuring expected credit losses to be consistent with its method for measuring expected credit losses for originated and purchased non-credit-deteriorated assets. Upon acquiring a PCD asset, the entity would recognize its allowance for expected credit losses as an adjustment that increases the cost basis of the asset (the "gross-up" approach). After initial recognition of the PCD asset and its related allowance, the entity would continue to apply the CECL model to the asset — that is, any changes in the entity's estimate of cash flows that it expects to collect (favorable or unfavorable) would be recognized immediately in the income statement. Interest income recognition would be based on the purchase price plus the initial allowance accreting to the contractual cash flows.

[4] The amendments do not apply to an AFS debt security that an entity intends to sell or will more likely than not be required to sell before the recovery of its amortized cost basis. If an entity intends to sell or will more likely than not be required to sell a security before recovery of its amortized costs basis, the entity would write down the debt security's amortized cost to the debt security's fair value as required under existing U.S. GAAP.

[5] The ASU defines PCD assets as "[a]cquired individual financial assets (or acquired groups of financial assets with similar risk characteristics) that, as of the date of acquisition, have experienced a more-than-insignificant deterioration in credit quality since origination, as determined by an acquirer's assessment."

Thinking It Through

Under current U.S. GAAP, an acquired asset is considered credit-impaired when it is probable that the investor would be unable to collect all contractual cash flows as a result of deterioration in the asset's credit quality since origination. Under the ASU, a PCD asset is an acquired asset that has experienced a more-than-insignificant deterioration in credit quality since origination. Consequently, entities will most likely need to use more judgment than they do under current guidance to determine whether an acquired asset has experienced significant credit deterioration.

Also, under the current accounting for purchased credit-impaired assets, an entity recognizes unfavorable changes in expected cash flows as an immediate credit impairment but treats favorable changes in expected cash flows that are in excess of the allowance as prospective yield adjustments. The CECL model's approach to PCD assets eliminates this asymmetrical treatment in cash flow changes. However, in a manner consistent with current practice, the CECL model precludes an entity from recognizing as interest income the discount embedded in the purchase price that is attributable to expected credit losses as of the date of acquisition.

Certain Beneficial Interests Within the Scope of ASC 325-40

Under the ASU, entities should measure an impairment allowance for purchased or retained beneficial interests in the same manner as PCD assets if the beneficial interest meets the definition of a PCD asset or there is a significant difference between the contractual cash flows and expected cash flows of the beneficial interest. At initial recognition, a beneficial interest holder would therefore present an impairment allowance equal to the estimate of expected credit losses.

Thinking It Through

Under the CECL model, an entity would be required to determine the contractual cash flows of beneficial interests in securitized transactions. However, the beneficial interests in certain structures may not have contractual cash flows (e.g., when a beneficial interest holder receives only residual cash flows of a securitization structure). In these situations, the entity may need to use a proxy for the contractual cash flows of the beneficial interest (e.g., the gross contractual cash flows of the underlying debt instrument).

Loan Commitments

Off-balance-sheet arrangements such as commitments to extend credit, guarantees, and standby letters of credit that are not considered derivatives under ASC 815 are subject to credit risk and are therefore within the scope of the CECL model. Accordingly, the ASU requires an entity's method for determining the estimate of expected credit losses on the *funded* portion of a loan commitment to be similar to its method for determining the estimate for other loans. For an *unfunded* portion of a loan commitment, an entity must estimate expected credit losses over the full contractual period over which the entity is exposed to credit risk under an unconditional present legal obligation to extend credit. Such an estimate takes into account both the likelihood that funding will occur and the expected credit losses on commitments to be funded.

Thinking It Through

An entity's estimate of expected credit losses on unfunded loan commitments (e.g., credit card receivables) will depend on (1) whether the entity has the unconditional ability to cancel the commitment to extend credit and, if so, (2) the time it takes for the cancellation to become effective. It is our understanding that if an entity has the unconditional ability to cancel the unfunded portion of a loan commitment, the entity would not be required to estimate expected credit losses on that portion, even if the entity has historically never exercised its cancellation right.

Disclosures

Many of the disclosures required under the ASU are similar to those already required under U.S. GAAP as a result of ASU 2010-20. Accordingly, entities must also disclose information about:

- Credit quality.[6]
- Allowances for expected credit losses.
- Policies for determining write-offs.
- Past-due status.
- Nonaccrual status.
- PCD assets.
- Collateral-dependent financial assets.

In addition, other disclosures are required as follows:

- Public business entities that meet the U.S. GAAP definition of an SEC filer[7] must disclose credit quality indicators disaggregated by year of origination for a five-year period.
- Public business entities that do not meet the U.S. GAAP definition of an SEC filer must disclose credit-quality indicators disaggregated by year of origination. However, upon adoption of the ASU, they would only be required to disclose such information for the previous three years, and would add another year of information each year after adoption until they have provided disclosures for the previous five years.
- Other entities are not required to disclose credit quality indicators disaggregated by year of origination.

Effective Date and Transition

Effective Date

For public business entities that meet the U.S. GAAP definition of an SEC filer, the ASU is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years.

[6] Short-term trade receivables resulting from revenue transactions within the scope of ASC 605 and ASC 606 are excluded from these disclosure requirements.

[7] Under U.S. GAAP, an SEC filer is defined as follows:

"An entity that is required to file or furnish its financial statements with either of the following:

a. The Securities and Exchange Commission (SEC)
b. With respect to an entity subject to Section 12(i) of the Securities Exchange Act of 1934, as amended, the appropriate agency under that Section.

Financial statements for other entities that are not otherwise SEC filers whose financial statements are included in submission by another SEC filer are not included within this definition."

For public business entities that do not meet the U.S. GAAP definition of an SEC filer, the ASU is effective for fiscal years beginning after December 15, 2020, including interim periods within those fiscal years.

For all other entities, the ASU is effective for fiscal years beginning after December 15, 2020, and interim periods within those fiscal years beginning after December 15, 2021.

In addition, entities are permitted to early adopt the new guidance for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years.

Transition Approach

For most debt instruments, entities must record a cumulative-effect adjustment to the statement of financial position as of the beginning of the first reporting period in which the guidance is effective (modified retrospective approach). However, the ASU provides the following instrument-specific transition guidance:

- *Other-than-temporarily impaired debt securities* — An entity is required to apply (1) the CECL model prospectively to HTM debt securities and (2) the changes to the impairment model for AFS debt securities prospectively. As a result, previous write-downs of a debt security's amortized cost basis would not be reversed; rather, only changes in the estimate of expected cash flows of the debt security occurring on or after the ASU's effective date would be reflected as an allowance for credit losses. Upon adoption of the new guidance, any impairment previously recognized in OCI would be accounted for as a prospective adjustment to the accretable yield of the debt instrument.
- *PCD assets* — An entity is required to apply the changes to PCD assets prospectively. That is, the change in the definition of a PCD asset applies only to assets acquired on or after the ASU's effective date. For debt instruments accounted for under ASC 310-30, an entity would apply the gross-up approach as of the transition date (i.e., establish an allowance for expected credit losses with a corresponding adjustment to the debt instrument's cost basis).

  In addition, an entity would immediately recognize any postadoption changes to its estimate of cash flows that it expects to collect (favorable or unfavorable) in the income statement as impairment expense (or reduction of expense). Accordingly, the yield on a PCD asset as of the date of adoption would be "locked" and would not be affected by subsequent changes in the entity's estimate of expected credit losses.
- *Certain beneficial interests within the scope of ASC 325-40* — Entities holding such interests need to comply with the same transition requirements as those that apply to PCD assets.

Thinking It Through

Financial institutions currently use various methods to estimate credit losses. Some apply simple approaches that take into account average historical loss experience over a fixed time horizon. Others use more sophisticated "migration" analyses and forecast modeling techniques. Under the CECL model, for any approach that is based solely on historical loss experience, an entity needs to consider the effect of forward-looking information over the remaining contractual life of a financial asset. In addition, as ASU 2016-13 states, "for periods beyond which the entity is able to make or obtain reasonable and supportable forecasts of expected credit losses, an entity shall revert to historical loss information determined in accordance with paragraph 326-20-30-8 that is reflective of the contractual term of the financial asset or group of financial assets."

For instance, assume that an entity uses annualized loss rates to determine the amount of probable unconfirmed losses on its homogeneous pools of loans as of the reporting date. When moving to the CECL model, the entity may need to revise its allowance method by adjusting the fixed time horizon (i.e., annualized loss rates) to equal a period that represents the full contractual life of the instrument. Entities using a probability-of-default (PD) approach may need to revise their PD and loss-given-default (LGD) statistics to incorporate the notion of lifetime expected losses. Today, an entity's PD approach might be an estimate of the probability that default will occur over a fixed assessment horizon, which is less than the full contractual life of the instrument (often one year). Similarly, an entity needs to revise its LGD statistic to incorporate the notion of lifetime expected losses (i.e., the percentage of loss over the total exposure if default were to occur during the full contractual life of the instrument).

Classification and Measurement

Background

ASU 2016-01 amends the guidance on the classification and measurement of financial instruments. The amendments contain changes related to the following:

- Accounting for equity investments (apart from those that are accounted for under the equity method or those that are consolidated).
- Recognition of changes in fair value attributable to changes in instrument-specific credit risk for financial liabilities for which the fair value option has been elected.
- Determining the valuation allowance for deferred tax assets (DTAs) related to AFS debt securities.
- Disclosure requirements for financial assets and financial liabilities.

For public business entities, the new standard is effective for fiscal years beginning after December 15, 2017, including interim periods therein. For all other entities, the standard is effective for fiscal years beginning after December 15, 2018, and interim periods within fiscal years beginning after December 15, 2019. Early adoption of certain of the standard's provisions is permitted for all entities. Nonpublic business entities are permitted to adopt the standard in accordance with the effective date for public business entities. For more information about ASU 2016-01, see Deloitte's January 12, 2016, *Heads Up*.

Classification and Measurement of Equity Investments

The amendments will require entities to carry all investments in equity securities at fair value, with changes in fair value recorded through earnings, unless the equity investments are accounted for under the equity method or are consolidated. For equity investments that do not have a readily determinable fair value, the guidance will permit a practicability exception under which the equity investment would be measured at cost less impairment, if any, plus or minus observable price changes in orderly transactions. This practicability exception would not be available to reporting entities that are investment companies, broker-dealers in securities, or postretirement benefit plans.

An entity that has elected the practicability exception for equity investments that do not have a readily determinable fair value is required to assess whether the equity investment is impaired by qualitatively considering the indicators described in ASC 321-10-35-3. If, on the basis of the qualitative assessment, the equity investment is impaired, an entity would be required to record an impairment equal to the amount by which the carrying value exceeds fair value. The entity should no longer evaluate whether such impairment is other than temporary.

Thinking It Through

Under current U.S. GAAP, marketable equity securities other than equity method investments or those that result in consolidation of the investee are classified as either (1) held for trading, with changes in fair value recognized in earnings, or (2) AFS, with changes in fair value recognized in OCI. Further, nonmarketable equity securities for which the fair value cannot be readily determined generally would be measured at cost (less impairment) unless the fair value option is elected. Under the new guidance, since equity securities can no longer be accounted for as AFS, entities holding such investments could see more volatility in earnings. Although applying the practicability exception to investments without readily determinable fair values may reduce such earnings volatility, this exception is not available to broker-dealers.

Changes in Fair Value of a Liability Attributed to Changes in Instrument-Specific Credit Risk

For financial liabilities (excluding derivative instruments) for which the fair value option has been elected, the amendments will require an entity to separately recognize in OCI any changes in fair value associated with instrument-specific credit risk. The guidance indicates that the portion of the total change in fair value that exceeds the amount resulting from a change in a base market risk (such as a risk-free interest rate) may be attributable to instrument-specific credit risk, but also acknowledges that there may be other methods an entity may use to determine instrument-specific credit risk.

Valuation Allowance on a DTA Related to an AFS Debt Security

The new guidance eliminates the diversity in practice related to the evaluation of the need for a valuation allowance for DTAs related to debt securities that are classified as AFS. Under current U.S. GAAP, entities may perform this evaluation either separately from their other DTAs or in combination with them. The new guidance clarifies that an entity should "evaluate the need for a valuation allowance on a [DTA] related to [AFS] securities in combination with the entity's other [DTAs]."

Changes to Disclosure Requirements

For nonpublic business entities, the amendments eliminate the requirement to disclose the fair value of financial instruments measured at amortized cost. In addition, for such financial instruments, public business entities would not be required to disclose (1) the information related to the methods and significant assumptions used to estimate fair value or (2) a description of the changes in the methods and significant assumptions used to estimate fair value. The guidance also clarifies U.S. GAAP by eliminating the provisions in ASC 825 that had been interpreted to permit an "entry" price notion for estimating the fair value of loans for disclosure purposes. The amendments require a public business entity to disclose the fair value in accordance with the exit price notion in ASC 820. In addition, all entities are required to disclose in the notes to the financial statement all financial assets and financial liabilities grouped by (1) measurement category (i.e., amortized cost or fair value — net income or OCI) and (2) form of financial asset (i.e., securities and loans/receivables).

Recognition of Breakage for Prepaid Stored-Value Products

Background

In March 2016, the FASB issued ASU 2016-04, which amended the guidance on extinguishing financial liabilities for certain prepaid stored-value products. Entities may sell prepaid stored-value products in physical and digital forms that can be redeemed by the holder to purchase goods or services. When an entity sells a prepaid stored-value product, it recognizes a liability to the product holder. As the holder redeems the prepaid stored-value product, the entity reduces its liability to the holder and settles its liability to the merchant that provided the goods or services. For various reasons, product holders may not use any, or a portion of, the product's prepaid value (commonly referred to as "breakage"). There is diversity in practice related to when an entity can derecognize the liability to the product holder as a result of breakage.

Scope

Prepaid stored-value products within the scope of ASU 2016-04 are those that are "commonly accepted as payment for goods or services" except for products that are:

- Within the scope of other U.S. GAAP topics (e.g., casino gaming chips[8] or revenue transactions).
- Part of customer loyalty programs.
- Subject to unclaimed property laws.
- Solely redeemable by the product holder for cash (however, a product that can be redeemed for cash and goods or services would be within the scope of the ASU).
- Attached to a segregated bank account (i.e., a customer deposit account).

Examples of products within the ASU's scope include traveler's checks, telecommunication cards, and money orders. Products not within its scope include bearer bonds, nonrecourse debt, and trade payables. Further, liabilities related to prepaid stored-value products within the scope of the ASU should be considered financial liabilities and should be accounted for consistently with the guidance in the new revenue standard (ASC 606) on breakage.

Thinking It Through

The scope of ASU 2016-04 excludes transactions that are accounted for under other U.S. GAAP topics, including revenue transactions. Prepaid stored-value products that are redeemable only from the issuer would generally be accounted for as a revenue transaction (from the issuer's perspective). It is our understanding that prepaid stored-value products that can be redeemed for goods or services from both the issuer and third-party merchants are within the scope of the ASU (from the issuer's perspective). For example, a prepaid stored-value product issuer may have corporate-owned locations as well as franchisee-owned locations. If a prepaid stored-value product can be used at both corporate- and franchisee-owned locations, the product would be within the scope of the ASU under the issuer's accounting.

Key Provisions of the ASU

If an entity selling prepaid stored-value products expects to be entitled to a breakage amount (i.e., an amount that will not be redeemed), the entity will recognize the effects of the expected breakage "in proportion to the pattern of rights expected to be exercised by the product holder only to the extent that it is probable that a significant reversal of the recognized breakage amount will not subsequently

[8] See ASC 924-405.

occur." That is, the entity would not recognize breakage immediately but rather proportionally as the prepaid stored-value product is being redeemed. Otherwise, the expected breakage would be recognized when the likelihood becomes remote that the holder will exercise its remaining rights.

Entities are required to reassess their estimate of breakage each reporting period. Any change in this estimate would be accounted for as a change in an accounting estimate.[9]

Thinking It Through

Under the guidance before the ASU, an entity may have continued to record a liability for unused prepaid stored-value products such as traveler's checks, telecommunication cards, and money orders in perpetuity if the entity had not been legally released from the liability. The ASU provides a scope exception from the guidance in ASC 405-20 such that entities selling these products no longer must be legally released from the obligation to derecognize a portion of the liability related to breakage.

Disclosure Requirements

An entity that recognizes breakage is required to disclose the "methodology used to recognize breakage and significant judgments made in applying the breakage methodology." Further, prepaid stored-value products within the scope of the ASU are excluded from the disclosure requirements in ASC 825 for financial liabilities.

Effective Date and Transition

For public business entities, the ASU is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. For all other entities, it is effective for annual periods beginning after December 15, 2018, and interim periods beginning after December 15, 2019. Early adoption is permitted, including adoption before the effective date of ASC 606. A reporting entity can apply the guidance by using either (1) a modified retrospective transition approach by recording a cumulative-effect adjustment to retained earnings as of the beginning of the annual period of adoption or (2) a full retrospective transition approach.

For more information about the ASU, see Deloitte's March 16, 2016, *Heads Up*.

Effect of Derivative Contract Novations on Existing Hedge Accounting

Background

In March 2016, the FASB issued ASU 2016-05, which clarifies the accounting for derivative contract novations on existing hedge accounting relationships. A derivative novation occurs when one party to the derivative contract assigns its rights and obligations to a new party (i.e., legally replaces itself with another party). Approval for the novation is typically required by the existing derivative counterparty. After the novation, the entity that was replaced by the new party no longer has any rights or obligations under the contract.

[9] See ASC 250-10-45-17 through 45-20.

Derivative novations can occur for various reasons, including the following:

- As a result of a financial institution merger, to designate the surviving entity as the new counterparty.
- As a vehicle for exiting a line of business or moving risk exposures between different legal entities of the same parent company.
- To satisfy laws or regulatory requirements (e.g., as a means of complying with requirements to use central derivative clearing counterparties).

Under ASC 815, an entity must discontinue a hedging relationship if (1) the hedging derivative instrument expires or is sold, terminated, or exercised or (2) it wishes to change a critical term of the hedging relationship. Before ASU 2016-05 was issued, ASC 815 did not, however, explicitly address how a novation of a hedging derivative affected a hedging relationship, and this ambiguity resulted in inconsistent application in practice.

ASU 2016-05 (codified in ASC 815) clarifies that "a change in the counterparty to a derivative instrument that has been designated as the hedging instrument in an existing hedging relationship would not, **in and of itself**, be considered a termination of the derivative instrument" (emphasis added) or "a change in a critical term of the hedging relationship." As long as all other hedge accounting criteria in ASC 815 are met, a hedging relationship in which the hedging derivative instrument is novated would not be discontinued or require redesignation. This clarification applies to both cash flow and fair value hedging relationships.

Key Provisions of the ASU

Thinking It Through

The Basis for Conclusions of ASU 2016-05 states that "a reporting entity always is required to assess the creditworthiness of the derivative instrument counterparty in a hedging relationship (both in the normal course of the hedging relationship and upon a novation)." Although an entity would not be required to discontinue the hedging relationship solely as a result of a change in counterparty, the entity would need to consider the counterparty's creditworthiness. If the new counterparty's creditworthiness differs significantly from that of the original counterparty, the hedging relationship may no longer be a highly effective hedge, which would trigger discontinuation of the hedged relationship.

Effective Date and Transition

For public business entities, the ASU is effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. For all other entities, it is effective for fiscal years beginning after December 15, 2017, and interim periods within fiscal years beginning after December 15, 2018. An entity would apply the guidance prospectively unless it elects modified retrospective transition. Early adoption is permitted, including in an interim period.

Prospective Approach

Under the prospective approach, an entity would apply the amendments only to hedging relationships in which a counterparty to the hedging derivative is changed after the date the reporting entity adopted ASU 2016-05.

Modified Retrospective Approach

If elected, the modified retrospective approach will apply to all derivative instruments that satisfy **all** of the following conditions:

- "The derivative instrument was outstanding during all or a portion of the periods presented in the financial statements."
- "The derivative instrument was previously designated as a hedging instrument in a hedging relationship."
- "The hedging relationship was dedesignated solely due to a novation of the derivative instrument, and all other hedge accounting criteria [in ASC 815] would have otherwise continued to be met."

For such hedging relationships, an entity would remove from the financial statements the effect of the hedge dedesignation that resulted from the novation for each period presented. The entity also would adjust beginning retained earnings to reflect the cumulative effect on the financial statements of derivatives that (1) meet the requirements above and (2) were dedesignated from hedging relationships as a result of novations that occurred before the beginning of the earliest period presented.

Thinking It Through

To apply the modified retrospective approach, an entity is required to assess hedge effectiveness and measure ineffectiveness as required by the original hedge documentation under ASC 815 for all periods between (1) the date on which the hedging relationship was dedesignated solely because of a novation and (2) the date on which the entity adopts ASU 2016-05.

Disclosure Requirements

Under either transition approach, an entity must provide the disclosures required by ASC 250-10-50-1(a) and 50-2 about the nature of and reason for the change in accounting principle, as applicable, in the period it adopts the ASU. An entity electing the modified retrospective approach must also provide the disclosures required by ASC 250-10-50-1(b)(1) and (b)(3) about the amounts retrospectively adjusted and the cumulative effect on retained earnings, as applicable.

Contingent Put/Call Options in Debt Instruments

To determine how to account for debt instruments with embedded features, including contingent put and call options, an entity is required to assess whether the embedded derivatives must be bifurcated from the host contract and accounted for separately. Part of this assessment consists of evaluating whether the embedded derivative features are clearly and closely related to the debt host. Before it was amended by ASU 2016-06, ASC 815-15 stated that contingently exercisable options had to be indexed only to interest rates or credit risk to be considered clearly and closely related to a debt host.

ASU 2016-06 was issued to address inconsistent interpretations of whether the event that triggers an entity's ability to exercise the embedded contingent option must be indexed to interest rates or credit risk for that option to qualify as clearly and closely related. Diversity in practice had developed because the four-step decision sequence in ASC 815-15-25-42 focused only on whether the payoff was indexed to something other than an interest rate or credit risk. As a result, entities were uncertain whether they should (1) determine whether the embedded features are clearly and closely related to the debt host solely on the basis of the four-step decision sequence or (2) first apply the four-step decision sequence

and then also evaluate whether the event triggering the exercisability of the contingent put or call option was indexed only to an interest rate or credit risk (and not some extraneous event or factor).

The ASU clarifies that in assessing whether an embedded contingent put or call option is clearly and closely related to the debt host, an entity is required to perform only the four-step decision sequence in ASC 815-15-25-42 as amended by the ASU. The entity does not have to separately assess whether the event that triggers its ability to exercise the contingent option is itself indexed only to interest rates or credit risk.

Effective Date and Transition

For public business entities, the ASU is effective for financial statements issued for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. For all other entities, it is effective for financial statements issued for fiscal years beginning after December 15, 2017, and interim periods beginning after December 15, 2018. An entity can early adopt the ASU, including in an interim period; however, if it early adopts in an interim period, it should reflect any adjustment as of the beginning of the fiscal year that includes the interim period.

An entity will apply a modified retrospective transition approach that requires it to use the four-step decision sequence to determine for existing debt instruments whether an embedded derivative is clearly and closely related to the debt host and to take into account the economic characteristics and risks of the host contract and the embedded option that existed on the date it issued or acquired the instrument.

If bifurcation of an embedded derivative is no longer required as a result of application of the ASU, the entity will determine the carrying amount of the debt instrument on the date of adoption as the aggregate of the carrying amount of the debt host contract and the fair value of the previously bifurcated embedded derivative. Any premium or discount resulting from such aggregation will not affect the entity's assessment of whether the call (put) option is clearly and closely related to the debt instrument. The entity will not make any cumulative-effect adjustments to beginning retained earnings.

An entity that is no longer required to bifurcate an embedded derivative from a debt instrument as a result of applying the guidance in the ASU also has a one-time option, as of the beginning of the fiscal year for which the amendments are effective, to irrevocably elect to measure that debt instrument in its entirety at fair value and recognize changes in fair value in earnings (if that instrument is within the scope of ASC 825-10-15-4 and 15-5). The effects of such an election would be reported as a cumulative-effect adjustment to the beginning retained earnings of the fiscal year of adoption. The entity should elect to apply the fair value option on an instrument-by-instrument basis.

See Deloitte's March 16, 2016, *Heads Up* for more information.

Leases

Background

After working for almost a decade, the FASB issued its new standard on accounting for leases, ASU 2016-02, in February 2016. The primary objective of issuing the new leases standard was to address the off-balance-sheet treatment of lessees' operating leases. The standard's lessee model requires lessees to adopt a right-of-use (ROU) asset approach that brings substantially all leases, with the exception of short-term leases (i.e., those with a lease term of less than 12 months), on the balance sheet. Under this

approach, a lessee would record an ROU asset representing its right to use the underlying asset during the lease term and a corresponding lease liability (in a manner similar to the current approach for capital leases).

The development of the new leases standard began as a convergence project between the FASB and the IASB. Although the project was a convergence effort and the boards conducted joint deliberations, there are several notable differences between the boards' respective leases standards.[10] One of the more significant differences is related to the classification of a lease. Under the FASB's standard, an entity may classify a lease as either an operating lease or a finance lease. Under the IASB's standard, however, an entity would classify all leases as finance leases.

Thinking It Through

ASU 2016-02 defines a lease as a "contract, or part of a contract, that conveys the right to control the use of identified property, plant, or equipment (an identified asset) for a period of time in exchange for consideration." While this definition may seem straightforward, judgment is crucial to identifying a complete population of leases. At first glance, a contract may not seem to meet a conventional understanding of a lease (e.g., a lease of a specific building). However, entities should evaluate their contracts and determine whether those contracts in their entirety or in part convey the right to use property, plant, or equipment. Because most leases will be recognized "on balance sheet" under the ASU, the financial statement implications of erroneously not identifying a lease in, for example, a service contract are far more significant than under ASC 840.

Lessee Accounting

While the boards agreed that a lessee should record an ROU asset and a corresponding lease liability when the lease commences, they supported different approaches for the lessee's subsequent accounting. The FASB chose a dual-model approach under which a lessee classifies a lease by using criteria similar to the lease classification criteria currently in IAS 17. Under IAS 17, there are no "bright lines" such as those under current U.S. GAAP (e.g., the 90 percent fair value test in ASC 840). For leases that are considered finance leases (many current capital leases are expected to qualify as finance leases), the lessee would account for the lease in a manner similar to a financed purchase arrangement. That is, the lessee would recognize interest expense and amortization of the ROU asset, which typically would result in a greater expense during the early years of the lease. For leases that are considered operating leases (many current operating leases are expected to continue to qualify as operating leases), the lessee would recognize a straight-line total lease expense. For both types of leases, the lessee would recognize an ROU asset for its interest in the underlying asset and a corresponding lease liability.

Lessor Accounting

The boards considered constituent feedback and decided not to make significant changes to the existing lessor accounting model. Rather, they agreed to adopt an approach that is similar to the existing capital/finance lease and operating lease models in ASC 840 and IAS 17. However, the FASB decided to align the U.S. GAAP classification requirements with the criteria in IAS 17. In addition, the FASB decided that for leases that are similar to current sales-type leases, the lessor would only be permitted to recognize the profit on the transaction if the arrangement would have qualified as a sale under the new revenue recognition guidance (ASC 606).

[10] The IASB issued IFRS 16, *Leases*, in January 2016.

The FASB also decided to eliminate leveraged-lease accounting for new arrangements. That is, while an entity may continue to account for a lease arrangement that commenced before the effective date of ASU 2016-02 as a leveraged lease under current guidance, a leveraged lease that is modified after the ASU's effective date would be accounted for as a new lease under the ASU's lessee and lessor models.

Thinking It Through

Capital and Covenant Considerations

Companies in the banking and securities sector have expressed concerns about the capital treatment of both the ROU asset and the associated liability recorded upon adoption of ASU 2016-02. Specifically, in the absence of clear FASB or SEC guidance, many expect regulators to view the ROU asset the same way they currently view a capital lease (i.e., not as a liquid asset). Regulators have not yet offered their views on how the ROU asset would affect a bank's common equity tier 1 capital. Constituents are therefore expecting additional clarification from the regulators to determine how the application of the guidance in the ASU would affect a bank's net capital computations.

Similarly, regulators have not yet determined what kind of relief, if any, would be granted to broker-dealers to avoid a 100 percent capital charge (e.g., whether a 100 percent capital charge would be required in the net capital computation for a broker-dealer institution since any illiquid asset is considered "nonallowable"). Further, for broker-dealers that use an aggregate indebtedness method to compute their net capital, the recognition of a leasing liability may increase the entity's aggregate indebtedness. Therefore, a broker-dealer lessee's net capital calculation and maximum debt-to-equity ratio calculated under Rule 15c3-1 of the Exchange Act may be adversely affected as a result of adoption of the ASU. As a result, holding companies would potentially be forced to make significant capital contributions to broker-dealer subsidiaries to ensure that the broker-dealers have sufficient capital to meet requirements.

Finally, as a result of the balance sheet gross-up required for lessees under the ASU, banking and securities lessees may need to adjust their existing loan covenants, which could trigger a broader renegotiation of the terms of, and revisions to, loan documentation.

Operational Considerations

To implement the lessee accounting requirements, banking and securities entities will have to collect and maintain data from all individual leases they are party to, including information related to real estate leases (e.g., ATM terminals and branches) and equipment leases. This data-gathering exercise may result in entity-wide operational challenges, particularly for entities with a global footprint. The new requirements could affect external as well as internal reporting information, including financial budgets and forecasts.

Entities that enter into intercompany service arrangements, which are often related to real estate, technology, or equipment, will need to determine whether these arrangements include lease components that may need to be accounted for in the separate-subsidiary financial statements. While the new leases standard requires entities to account for intercompany lease arrangements on the basis of the arrangements' legal form (rather than their substance), the administrative burden related to inventorying such contracts may be significant.

Effective Date and Transition

ASU 2016-02 is effective for public business entities for annual years beginning after December 15, 2018, including interim periods therein. For all other entities, the standard is effective for annual periods beginning after December 15, 2019, and interim periods thereafter. Early adoption is permitted. Lessees and lessors are required to use a modified retrospective transition method for existing leases. Accordingly, they would apply the new accounting model for the earliest year presented in the financial statements.

For discussion of additional implementation considerations, see Deloitte's March 1, 2016, *Heads Up*.

Revenue Recognition

Background

In May 2014, the FASB issued ASU 2014-09, which outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance (e.g., certain sections of ASC 360-20 and ASC 970-605). For additional information about ASU 2014-09 as issued, see Deloitte's May 28, 2014, *Heads Up* and July 2014 *Financial Services Spotlight*.

In response to concerns the FASB received related to applying the ASU's requirements, the Board in 2016 issued the following four ASUs, which amend the ASU's new revenue recognition guidance:

- *ASU 2016-08,* Principal Versus Agent Considerations (Reporting Revenue Gross Versus Net) — The ASU addresses issues related to how an entity should assess whether it is the principal or the agent in contracts that include three or more parties. The amendments provide guidance on (1) how to determine the unit of account, (2) whether the indicators in ASU 2014-09 are intended to help entities perform a single evaluation of control or represent an additional evaluation, and (3) how certain indicators are related to the general control principle. The ASU also clarifies that an entity should evaluate whether it is the principal or the agent for each good or service specified in a contract and thus whether an entity could be both the principal and agent for different performance obligations in the same contract. See Deloitte's March 22, 2016, *Heads Up* for more information.
- *ASU 2016-10,* Identifying Performance Obligations and Licensing — The ASU's amendments clarify the guidance on an entity's identification of certain performance obligations. Changes include guidance on immaterial promised goods and services and separately identifiable promises as well as (1) a policy election for shipping and handling fees incurred after control transfers and (2) clarifications related to licenses. See Deloitte's April 15, 2016, *Heads Up* for more information.
- *ASU 2016-11,* Rescission of SEC Guidance Because of Accounting Standards Updates 2014-09 and 2014-16 Pursuant to Staff Announcements at the March 3, 2016 EITF Meeting (SEC Update) — The ASU rescinds the following guidance, which is based on announcements made by the SEC staff at the Emerging Issues Task Force's (EITF's) March 3, 2016, meeting, upon an entity's adoption of ASU 2014-09:
    - Revenue and expense recognition for freight services in process (ASC 605-20-S99-2).
    - Accounting for shipping and handling fees and costs (ASC 605-45-S99-1).
    - Accounting for consideration given by a vendor to a customer (ASC 605-50-S99-1).

  - Accounting for gas-balancing arrangements (ASC 932-10-S99-5).
- *ASU 2016-12,* Narrow-Scope Improvements and Practical Expedients — The guidance (1) clarifies how to assess whether collectibility is probable in certain circumstances to support the existence of a contract, (2) adds a practical expedient for the presentation of sales taxes on a net basis in revenue, (3) clarifies how to account for noncash consideration at contract inception and throughout the contract period, and (4) establishes a practical expedient to address contract modifications upon transition. See Deloitte's May 11, 2016, *Heads Up* for more information.

In addition to the ASUs above, the FASB on May 18, 2016, and September 19, 2016, issued proposed ASUs that would make technical corrections (i.e., minor changes and improvements) to certain aspects of ASU 2014-09 related to the following topics:

- *Contract costs — impairment testing* — The proposed amendments "would clarify that when performing impairment testing an entity should (a) consider expected contract renewals and extensions and (b) include both the amount of consideration it already has received but has not recognized as revenue and the amount the entity expects to receive in the future."
- *Disclosure of remaining performance obligations* — The proposed amendments would (1) "provide practical expedients to the disclosure requirement for remaining performance obligations for specific situations in which an entity need not estimate variable consideration in order to recognize revenue" and (2) "expand the information disclosed when an entity applies one of the practical expedients."
- *Contract modifications example* — The proposed amendments "would improve the alignment of Example 7 and the [contract modifications] principles in Topic 606."
- *Cost capitalization for advisers to private and public funds* — The proposed amendments "would align the cost-capitalization guidance for advisors to both public funds and private funds in Topic 946."
- *Loan guarantee fees* — The proposed amendments "would clarify that guarantee fees within the scope of Topic 460 (other than product or service warranties) are not within the scope of Topic 606."
- *Contract asset versus receivable* — The proposed amendments "would provide a better link between the analysis in Example 38, Case B and the receivables presentation guidance in Topic 606."
- *Advertising costs* — The proposed amendments "would reinstate the guidance on the accrual of advertising costs."

The amendments are being proposed in response to feedback received from several sources, including the TRG for revenue recognition, and would clarify, rather than change, the new revenue standard's core revenue recognition principles. The Board discussed the proposed technical corrections at its August 31, 2016, and October 19, 2016, meetings. See Deloitte's September 1, 2016, and October 21, 2016, journal entries for more information on the Board's discussions.

Thinking It Through

Depository Institutions

One of the major implementation challenges for banks and other financial institutions has been determining whether a transaction is within the scope of ASC 606. Such a determination requires careful consideration of the facts and circumstances and must be well documented. To date, transactions that have seemed to garner the most attention include the following:

- *Deposit-related fees and ATM usage fees* — Under current U.S. GAAP, there is no explicit industry guidance on the deposit-related fees charged to customers by banks, such as account maintenance fees (which may be charged when a customer does not keep a required minimum balance in the deposit account) and ATM usage fees. The new revenue standard excludes from its scope transactions that are accounted for under other ASC topics, including those within the scope of ASC 405 (liabilities), ASC 460 (guarantees), ASC 815 (derivatives and hedging), and ASC 860 (transfers and servicing). As a result, stakeholders have questioned whether such fees are within the scope of ASC 606.

  At the April 2016 TRG meeting, the FASB staff addressed this scope issue by noting that entities would account for revenue from deposit-related fees in accordance with ASC 606 after they adopt the new standard. Financial institutions would continue to (1) record liabilities for customer deposits because the deposits meet the definition of a liability and (2) account for customer deposits in accordance with ASC 405. However, because ASC 405 does not contain specific guidance on how to account for deposit fees, financial institutions should apply ASC 606 for deposit-related fees (i.e., in a manner similar to the application of existing SEC revenue guidance by some financial institutions to account for deposit-related fees). The FASB staff suggested that implementation concerns raised by some stakeholders could be alleviated by careful analysis of the contract terms between the financial institution and the customer. Because customers generally have the right to cancel their depository arrangement at any time, the FASB staff believes that most contracts would be short term (e.g., day to day or minute to minute). Therefore, revenue recognition patterns would be similar regardless of the number of performance obligations identified, and any changes to current practice would most likely be insignificant.

- *Mortgage servicing rights* — As noted above, the new revenue standard excludes from its scope transactions that are accounted for under other ASC topics, including those within the scope of ASC 405 (liabilities), ASC 460 (guarantees), ASC 815 (derivatives and hedging), and ASC 860 (transfers and servicing). To determine which guidance applies to the fees associated with certain common financial institution transactions, stakeholders have asked the FASB to clarify whether mortgage servicing rights should be accounted for under ASC 606 or ASC 860. At the April 2016 TRG meeting, the FASB staff noted that assets and liabilities associated with mortgage servicing rights traditionally have been accounted for under ASC 860 and that such practice will not change under the new revenue standard. The staff believes that servicing arrangements that are within the scope of ASC 860 are not within the scope of ASC 606 and that ASC 860 addresses both the initial recognition and subsequent measurement of mortgage servicing assets and liabilities. In the staff's view, since the subsequent measurement of the mortgage servicing assets and liabilities depends on the cash flows associated with the mortgage servicing rights, ASC 860 should be used to account for such cash flows.

- *Loan origination fees* — Many stakeholders believe that loan origination fees are not within the scope of ASC 606 (much like their status under the revenue guidance before ASU 2014-09). Rather, such charges are considered lending-related fees because they are associated with contractual rights and obligations that are addressed in ASC 310. In addition, many believe that other lending-related fees, including interest income on receivables, rebates of accrued interest income, prepayment charges, delinquency charges (late fees), and loan commitment fees, would not be subject to ASC 606.
- *Bank-issued credit card fees and related reward programs* — Under current U.S. GAAP, credit card arrangements are typically accounted for under ASC 310. ASC 606 notes that financial instruments within the scope of other ASC topics, including ASC 310, are excluded from the scope of the new revenue standard unless those other ASC topics "do not specify how to separate and/or initially measure one or more parts of the contract."[11] Stakeholders have questioned whether credit card arrangements generally — or specific features of such arrangements — are within the scope of the new revenue standard since the arrangements often involve different (1) fees (e.g., annual fees, late fees), (2) features (e.g., concierge services, rewards programs), and (3) parties to the transaction (e.g., issuer, cardholder, network, merchant, merchant acquirer). At the July 13, 2015, TRG meeting, members of the TRG agreed with the FASB staff that because the new revenue standard does not include consequential amendments to ASC 310, entities should continue to account for services exchanged for credit card fees under ASC 310 rather than ASC 606. However, there was also general agreement that entities should, as an anti-abuse measure, assess whether the issuance of a credit card appears incidental to the arrangement (which potentially requires the arrangement to be within the scope of ASC 606). In addition, cardholder rewards programs would generally be within the scope of ASC 310 if the credit card arrangement is within the scope of ASC 310.
- *Bundled arrangements* — ASC 606-10 provides certain scope exceptions for contracts with customers that are within the scope of other topics, including contracts involving financial instruments. However, ASC 606-10 also provides guidance on assessing contracts that are partially within the scope of another topic and partially within the scope of ASC 606, thus indicating that certain arrangements involving financial instruments may be at least partially subject to the new revenue recognition guidance. ASC 606-10-15-4 describes the method entities should use to separate parts of a contract into those subject to ASC 606 and those subject to other topics. This is a departure from current U.S. GAAP, under which financial institutions are not subject to the multiple-element guidance in ASC 605-25 for bundling arrangements that provide both services and financial instruments to customers. Currently, therefore, entities generally do not consider concepts such as vendor-specific objective evidence when evaluating such contracts. Under ASC 606, entities are required to first apply the separation and measurement guidance in other ASC topics before applying the guidance in ASC 606. As a result, any discount inherent in the contract would be allocated to the part of the contract that is subject to ASC 606 since this is the last part to be separated and measured.

[11] See ASC 606-10-15-2 through 15-5 for additional information.

Example — Bundled Arrangements

A bank with an investment management division that sponsors a fund for which it acts as a general partner and investment manager may be partially within the scope of ASC 606 depending on the nature of the services and instruments it provides to its customers. For example, under the terms of an investment management agreement, the bank receives a management fee based on total assets managed and a performance fee based on excess returns once investors have earned a specific return rate. The bank must also hold a small equity investment in the fund. In these circumstances (and as long as the bank is not required to consolidate the fund in accordance with ASC 810), the bank would need to evaluate each involvement with the fund separately to determine which activities, if any, are within the scope of ASC 606 and other ASC topics. For instance, the equity ownership in the fund may be subject to the guidance in ASC 323 but management and performance-related fees are likely to be subject to the guidance in ASC 606.

Broker-Dealers

While ASU 2014-09 is expected to affect broker-dealers in many ways, the treatment of revenue from financial instruments (i.e., interest and dividend income) is not likely to change because such contracts are subject to the guidance in ASC 310-940 and ASC 320-940 and are specifically outside the scope of ASC 606.

For example, ASU 2014-09 is expected to affect the treatment of commission income earned by a clearing broker-dealer, which is within the scope of ASC 606. Some of the more significant issues broker-dealers will face as they analyze contracts to determine the appropriate treatment under the new guidance are as follows:

- *Identifying performance obligations* — In step 2 of the revenue model, entities are required to identify distinct performance obligations (i.e., deliverables from which the customer can benefit either on its own or together with other resources that are readily available to the customer and separately identifiable from other items in the contract). Typical goods and services provided in contracts between a clearing broker-dealer and its customers include trade execution, clearing services, and custody services. It is unlikely that trade execution and clearing services would be separately identifiable since they are both required services for security trading. Rather, these two services are expected to be combined and identified as one performance obligation in most cases. Custody services, however, are likely to be separately identifiable since a customer can benefit from these services separately from the trade execution and clearing services. Entities would similarly need to evaluate investment research services, which are common in arrangements with broker-dealers.
- *Determining when performance obligations are satisfied* — Generally, the commissions charged by the broker-dealer to the customer upon trade execution are the only fees charged and therefore represent the transaction price for the trade execution, clearing, and custody services. Revenue recognition related to such fees would occur on the trade date since that is the date on which (1) the broker-dealer is performing the service and has a present right to payment and (2) the customer receives the benefits of the underlying security (for purchases) or is no longer subject to the risk of changes in value (for sales). Additional analysis related to determining when performance obligations are satisfied is required for contracts that are fixed in duration or contain fees specifically for custody-related services such as processing and handling of legal documents.

Other broker-dealer transactions that may be affected by ASU 2014-09 and that are still under evaluation include (1) selling and distribution fees, (2) investment banking advisory fees, (3) underwriting revenues, (4) soft-dollar arrangements, (5) costs associated with underwriting and advisory services (i.e., principal versus agent treatment), (6) volume-related discounts on trades, and (7) free trades (e.g., when a minimum number of trades is executed or in exchange for accounts opened that exceed certain dollar thresholds).

These and other issues are the subjects of several papers written by the AICPA's Depository Institutions and Broker-Dealers Revenue Recognition task forces. See the AICPA's Web site for a list of the issues on the task forces' agendas for discussion and their respective statuses.

Accounting for Real Estate Sales Under the New Revenue Standard

ASU 2014-09 supersedes most of the current revenue recognition guidance under U.S. GAAP, including the guidance on real estate derecognition for most transactions.[12] While many constituents will be relieved that the ASU eliminates the current bright-line guidance in ASC 360-20 on when to derecognize real estate assets, entities may be required to reassess their historical accounting for real estate disposals.

Thinking It Through

Banks that foreclose on collateralized loans are currently required to apply ASC 360-20 to evaluate when they can derecognize their "real estate owned" when they subsequently sell the foreclosed assets. ASU 2014-09 eliminates the requirements in ASC 360-20 related to assessing (1) the adequacy of a buyer's initial and continuing investments and (2) the seller's continuing involvement with the property. When banks evaluate whether they can derecognize real estate under the new standard, they will need to assess whether it is "probable" that they will collect the consideration to which they will be entitled in exchange for transferring the asset(s) to the customer. In addition, rather than preventing derecognition, a seller's postsale involvement with the disposed asset may need to be accounted for as a separate performance obligation.

Financing Arrangements (Existence of a Contract)

Under current guidance, when the seller of real estate also provides financing to the buyer, the seller must consider the buyer's initial and continuing investments in the property to determine whether they constitute a stake sufficient to ensure that the risk of loss will motivate the buyer to honor its obligation to the seller. If the specified investment requirements are not met, the seller accounts for the sale by using the installment method, the cost recovery method, or the deposit method.

Under ASU 2014-09, an entity will need to evaluate several criteria to determine whether a contract exists. One particularly challenging criterion related to evaluating whether a real estate contract exists is that it must be "probable that the entity will collect the consideration to which it will be entitled." To make this determination, the entity should consider the buyer's ability and intention to pay the amount of consideration when it is due. The ASU does not retain the specific initial and continuing investment thresholds under current U.S. GAAP related to performing this evaluation; however, some factors to consider may include the loan-to-value ratio of the property and the purchaser's intended use of it.

[12] While the ASU eliminates the guidance in ASC 360-20 on real estate sales, there could be circumstances in which a transaction would have qualified for a sale under the previous leases guidance but will not qualify for a sale under ASC 606, or vice versa. In particular, many sale-and-leaseback transactions involving real estate will qualify for sale-and-leaseback accounting that would not have qualified for such accounting under the previous leases guidance.

Thinking It Through

The collectibility criterion should be evaluated on the basis of the amount to which the entity expects to be entitled, which may not be the stated transaction price. For example, these two amounts may differ because an entity anticipates offering the customer a price concession. Accordingly, an entity should carefully assess the facts and circumstances to determine whether, on the basis of its assessment of the customer's credit risk, for example, the entity expects to grant a price concession.

If a seller determines that a contract does not exist, it would account for any amounts received as a deposit (even if such payments are nonrefundable). In addition, the seller would continually evaluate the amounts received to determine whether the arrangement subsequently qualifies as a valid contract under the ASU's criteria. Once it becomes probable that the seller will collect the consideration to which it will be entitled, the seller would evaluate the arrangement under the derecognition criteria in the ASU. If, instead, the contract is terminated, the seller would then recognize any nonrefundable deposits received as a gain.

Identifying and Satisfying Performance Obligations

Sometimes, a seller remains involved with property that has been sold (e.g., by providing additional services such as construction or development activities). Under current guidance, profit is generally deferred if a seller has continuing involvement with the sold property. Sometimes, instead of accounting for the transaction as a sale, the seller may be required to (1) apply the deposit method to the transaction or (2) account for the transaction as a financing, leasing, or profit-sharing arrangement. The guidance before ASU 2014-09 focuses on whether the seller retains substantial risks or rewards of ownership as a result of its continuing involvement with the sold property.

By contrast, under the ASU, if the arrangement includes ongoing involvement with the property, the seller must evaluate each promised good or service under the contract to determine whether it represents a "separate performance obligation," constitutes a guarantee, or prevents the transfer of control.[13] Goods and services are distinct (and considered separate performance obligations) if the two criteria in ASC 606-10-25-19 are met, including the requirement that goods or services are distinct in the context of the contract. Alternatively, an entity would bundle goods or services until they are distinct. Further, ASC 606-10-25-21 provides guidance on when goods or services would be distinct in the context of the contract.

If a promised good or service is considered a separate performance obligation, an allocated portion of the transaction price should be recognized as revenue when (or as) the entity transfers the related good or service to the customer.

Partial Sales

In June 2016, the FASB issued a proposed ASU that would clarify the scope of the Board's recently established guidance on nonfinancial asset derecognition (ASC 610-20) as well as the accounting for partial sales of nonfinancial assets. The proposed guidance is in response to stakeholder feedback indicating that (1) the meaning of the term "in-substance nonfinancial asset" is unclear because the Board's new revenue standard does not define it and (2) the scope of the guidance on nonfinancial assets is complex and does not specify how a partial sales transaction should be accounted for or which model entities should apply.

[13] Certain forms of continuing involvement would not constitute a separate performance obligation. For example, an option or obligation to repurchase a property is specifically addressed by the ASU and would preclude derecognition of the property. Further, a seller obligation that qualifies as a guarantee under ASC 460 would be outside the scope of the ASU.

"Partial sales" are sales or transfers of a nonfinancial asset to another entity in exchange for a noncontrolling ownership interest in that entity. See the discussion of the FASB's proposal to clarify the accounting for partial sales of nonfinancial assets in the Accounting for Partial Sales of Nonfinancial Assets section below.

Effective Date and Transition

In August 2015, as a result of stakeholder concerns, the FASB issued ASU 2015-14, which delays the effective date of ASU 2014-09. Accordingly, the ASU is effective for public business entities for annual reporting periods (including interim reporting periods within those periods) beginning after December 15, 2017. Early adoption is permitted as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within those annual periods.

For nonpublic entities, the standard is effective for annual reporting periods beginning after December 15, 2018, and interim reporting periods within annual reporting periods beginning after December 15, 2019. Nonpublic entities can also elect to early adopt the standard as of the following:

- Annual reporting periods beginning after December 15, 2016, including interim periods.
- Annual reporting periods beginning after December 15, 2016, and interim periods within annual reporting periods beginning one year after the annual reporting period of initial application of the new standard.

Implementation and Transition Activities

A number of groups are involved in implementation activities related to the new standard, including the TRG (see Deloitte's *TRG Snapshot* newsletters), the AICPA's revenue recognition task forces, various firms, the SEC,[14] and the PCAOB. Preparers should continue to monitor the activities of these groups before adoption of the new guidance. See Deloitte's January 14, 2016, *Heads Up* for additional adoption and transition observations.

Simplifying the Transition to the Equity Method of Accounting

The FASB issued ASU 2016-07 in March 2016 as part of its simplification initiative. Under the guidance in U.S. GAAP before the ASU's amendments, an investor that meets the conditions for applying the equity method of accounting is required to retrospectively apply such method to all prior periods in which it had historically accounted for the investment under the cost method or as an AFS security. The ASU removes the requirement to retrospectively apply the equity method of accounting. It also requires entities to recognize unrealized holding gains or losses in accumulated other comprehensive income related to an AFS security that becomes eligible for the equity method of accounting in earnings as of the date the investment qualifies for the equity method of accounting.

The guidance is effective for all entities for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. The guidance must be applied prospectively to increases in the level of ownership interest or degree of influence occurring after the ASU's effective date. Early adoption is permitted.

[14] The SEC has indicated that it plans to review and update the revenue recognition guidance in SAB Topic 13 in light of the ASU. The extent to which the ASU's guidance will affect a public entity will depend on whether the SEC removes or amends the guidance in SAB Topic 13 to be consistent with the new revenue standard.

Also as part of its simplification initiative, the FASB issued a proposed ASU in June 2015 that would have eliminated the requirement to separately account for basis differences (i.e., the difference between the cost of an investment and the amount of underlying equity in net assets). The proposed guidance would have also eliminated the requirement for an investor to allocate basis differences to specific assets and liabilities of the investee and account for them accordingly (e.g., additional depreciation for basis differences assigned to tangible assets). However, many commenters on the proposed ASU indicated that eliminating the allocation of basis differences could create different complexities and result in inflated values of investments that would no longer be amortized over time as well as increase the likelihood of impairment in future periods. Accordingly, in May 2016, the FASB decided to remove the project from its agenda because of "insufficient support to change the equity method of accounting."

Thinking It Through

Application of the existing accounting requirements (i.e., before the ASU's amendments) can be particularly onerous because investments are often structured as partnerships or limited liability corporations, which may require use of the equity method at a relatively low ownership percentage. Further, investments in specific securities may evolve over time, depending on investment strategy and portfolio allocation. For public companies, the existing U.S. GAAP requirements have been compounded by the SEC's guidance requiring registrants to provide (1) separate or summarized financial statements for prior periods once the equity method of accounting is applied to a significant investment (see paragraph 2405.5 of the SEC's *Financial Reporting Manual*) or (2) retroactively adjusted annual financial statements reflecting the equity method of accounting if a registration statement is filed after the first quarter in which the change to the equity method of accounting is reported but before the next annual report on Form 10-K is filed (see Topic 13 of the *Financial Reporting Manual*).

Accordingly, the ASU provides welcome relief from complex accounting considerations and SEC reporting requirements related to a transition to the equity method of accounting. However, the new ASU will also introduce new complexities after such transition. For example, application of the new method may result in additional basis differences if the earnings that would have affected the cost basis under existing U.S. GAAP are not recognized retrospectively.

Consolidation — Interests Held Through Related Parties That Are Under Common Control

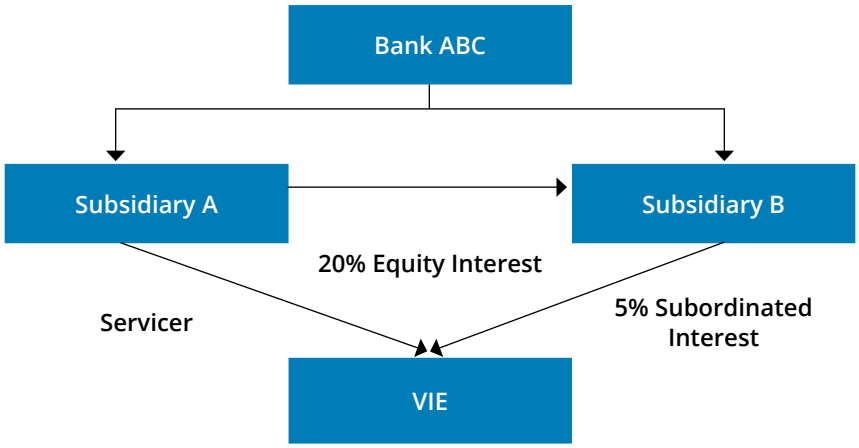
Background

In February 2015, the FASB issued ASU 2015-02, which amends the guidance in ASC 810-10 to require, among other things, a reporting entity that is a single decision maker to consider interests held by its related parties only if the reporting entity has a direct interest in the related parties. If the related parties and the reporting entity are not under common control, the indirect economic interests in a variable interest entity (VIE) held through related parties would be considered on a proportionate basis in the determination of whether the reporting entity is the primary beneficiary of the VIE. Alternatively, if the related parties and the reporting entity are under common control, the reporting entity would be required to consider the interests of the related parties in their entirety (not on a proportionate basis). As a result, the reporting entity may satisfy the "power" criterion (i.e., the ability to direct the activities that most significantly affect the VIE's economic performance) in the consolidation analysis even if it has a relatively insignificant economic interest in the VIE.

In October 2016, the FASB issued ASU 2016-17 to remove the last sentence of ASC 810-10-25-42, which states, "Indirect interests held through related parties that are under common control with the decision maker should be considered the equivalent of direct interests in their entirety." As a result of the ASU, a reporting entity would consider its indirect economic interests in a VIE held through related parties that are under common control on a proportionate basis in a manner consistent with its consideration of indirect economic interests held through related parties that are not under common control.

Example

Bank ABC establishes a trust (a VIE) to securitize financial assets. The VIE has a servicer (Subsidiary A) that does not hold any of the beneficial interests in the trust. Subsidiary B holds a 5 percent interest in the trust, which represents the most subordinated interest and therefore absorbs more than an insignificant amount of the expected losses of the trust. Various unrelated investors hold the remaining beneficial interests. In addition, A holds a 20 percent interest in B, and both entities are wholly owned subsidiaries of Bank ABC. As the servicer, A has full discretion to service the financial assets, and it was determined that decisions related to the financial assets are the most significant decisions of the trust.



Under the guidance before ASU 2016-17, A and B must consider their own interests before evaluating which entity is the primary beneficiary of the VIE. Accordingly, A would conclude that it meets the power criterion as well as the economics criterion (i.e., the obligation to absorb losses of the VIE that could potentially be significant to the VIE or the right to receive benefits from the VIE that could potentially be significant to the VIE) on its own because A must treat B's subordinated interest in the VIE as its own as a result of A's interest in B, and the entities are under common control of Bank ABC.

Under the ASU, A will still conclude that it meets the power criterion on its own. However, in the evaluation of the economics criterion, since A owns a 20 percent interest in B, and B owns a 5 percent subordinated interest in the VIE, Subsidiary A will conclude that it has a 1 percent indirect interest in the VIE a result of its interest in B (20 percent interest in B multiplied by B's 5 percent interest in the VIE). Therefore, A will be unlikely to meet the economics criterion on its own. However, since A and B are under common control and as a group will satisfy the power and economics criteria, they will need to perform the related-party tiebreaker test to determine which party is most closely associated with the VIE.

Thinking It Through

As a result of the ASU, the related-party tiebreaker test will be performed more frequently because, as illustrated in the example above, it will be less likely for the decision maker to meet the economics criterion on its own when considering its exposure through a related party under common control on a proportionate basis.[15] Many decision makers view the ASU's guidance favorably because they would otherwise consolidate a legal entity with a small indirect interest. The ASU will instead require the decision maker to consider which party (the single decision maker or the related party under common control) is most closely associated with the VIE and therefore should consolidate. This guidance may have a significant impact on the individual financial statement of banking and securities subsidiaries because it could change which subsidiary consolidates a VIE.

Effective Date and Transition

For all reporting entities, the guidance will be effective for annual periods beginning after December 15, 2016. Reporting entities that have not yet adopted the guidance in ASU 2015-02 will be required to adopt ASU 2016-17's amendments at the same time they adopt those in ASU 2015-02. Early adoption, including adoption in an interim period, is permitted as of October 26, 2016 (the ASU's issuance date).

Employee Share-Based Payment Accounting Improvements

Background

In March 2016, the FASB issued ASU 2016-09, which simplifies several aspects of the accounting for employee share-based payment transactions for both public and nonpublic entities, including the accounting for income taxes, forfeitures, and statutory tax withholding requirements, as well as classification in the statement of cash flows. The new guidance, which is part of the Board's simplification initiative, also contains practical expedients for nonpublic entities.

Key Provisions of the ASU

Accounting for Income Taxes

Under current guidance, when a share-based payment award is granted to an employee, the fair value of the award is generally recognized over the vesting period, and a corresponding DTA is recognized to the extent that the award is tax-deductible. The tax deduction is generally based on the intrinsic value at the time of exercise (for an option) or on the fair value upon vesting of the award (for restricted stock), and it can be either greater (excess tax benefit) or less (tax deficiency) than the compensation cost recognized in the financial statements. All excess tax benefits are recognized in additional paid-in capital (APIC), and tax deficiencies are recognized either in the income tax provision or in APIC to the extent that there is a sufficient "APIC pool" related to previously recognized excess tax benefits.

[15] This outcome is because the FASB has proposed to change only the guidance in ASC 810-10-25-42. The Board also considered amending the guidance on determining whether fees paid to a decision maker or service provider represent a variable interest in the evaluation of a decision maker's indirect interests held through related parties under common control. While the proposal would retain that guidance, the Board will consider clarifying it, as well as other aspects of the guidance on common-control arrangements, as part of a separate initiative. The proposal therefore only affects the decision maker's consideration of indirect interests held through related parties under common control in the primary-beneficiary assessment.

Under the ASU, an entity recognizes all excess tax benefits and tax deficiencies as income tax expense or benefit in the income statement. This change eliminates the notion of the APIC pool and significantly reduces the complexity and cost of accounting for excess tax benefits and tax deficiencies. In addition, excess tax benefits and tax deficiencies are considered discrete items in the reporting period in which they occur and are not included in the estimate of an entity's annual effective tax rate.

The ASU's guidance on recording excess tax benefits and tax deficiencies in the income statement also has a corresponding effect on the computation of diluted earnings per share (EPS) when an entity applies the treasury stock method. An entity that applies such method under current guidance estimates the excess tax benefits and tax deficiencies to be recognized in APIC in determining the assumed proceeds available to repurchase shares. However, under the ASU, excess tax benefits and tax deficiencies are excluded from the calculation of assumed proceeds since such amounts are recognized in the income statement. In addition, the new guidance affects the accounting for tax benefits of dividends on share-based payment awards, which will now be reflected as income tax expense or benefit in the income statement rather than as an increase to APIC.

Further, the ASU eliminates the requirement to defer recognition of an excess tax benefit until the benefit is realized through a reduction to taxes payable.

In addition to addressing the recognition of excess tax benefits and tax deficiencies, the ASU provides guidance on the related cash flow presentation. Under existing guidance, excess tax benefits are viewed as a financing transaction and are presented as financing activities in the statement of cash flows. However, there is no cash receipt but only a reduction in taxes payable. Therefore, a reclassification is made in the statement of cash flows to reflect a hypothetical inflow in the financing section and a hypothetical outflow from the operating section.

Under the ASU, excess tax benefits no longer represent financing activities since they are recognized in the income statement; therefore, excess tax benefits are not separate cash flows and should be classified as operating activities in the same manner as other cash flows related to income taxes. Accordingly, the ASU eliminates the requirement to reclassify excess tax benefits from operating activities to financing activities.

Accounting for Forfeitures

The ASU allows an entity to elect as an accounting policy either to continue to estimate the total number of awards for which the requisite service period will not be rendered (as currently required) or to account for forfeitures when they occur. This entity-wide accounting policy election only applies to service conditions; for performance conditions, the entity continues to assess the probability that such conditions will be achieved. An entity must also disclose its policy election for forfeitures.

Thinking It Through

An entity that adopts a policy to account for forfeitures as they occur must still estimate forfeitures when an award is (1) modified (the estimate applies to the original award in the measurement of the effects of the modification) and (2) exchanged in a business combination (the estimate applies to the amount attributed to precombination service). However, the accounting policy for forfeitures will apply to the subsequent accounting for awards that are modified or exchanged in a business combination.

Statutory Tax Withholding Requirements

The ASU modifies the current exception to liability classification of an award when an employer uses a net-settlement feature to withhold shares to meet the employer's minimum statutory tax withholding requirement. Currently, the exception only applies when no more than the number of shares necessary for the minimum statutory tax withholding requirement to be met is repurchased or withheld. The new guidance stipulates that the net settlement of an award for statutory tax withholding purposes would not result, by itself, in liability classification of the award provided that the amount withheld for taxes does not exceed the maximum statutory tax rate in the employees' relevant tax jurisdictions.

Further, to eliminate diversity in practice, the ASU requires that cash payments to tax authorities in connection with shares withheld to meet statutory tax withholding requirements be presented as a financing activity in the statement of cash flows because such payments represent an entity's cash outflow to reacquire the entity's shares.

Thinking It Through

Under current guidance, an entity is required to track the minimum statutory tax withholding requirement applicable to each specific award grantee in each applicable jurisdiction if shares are repurchased or withheld. Under the new guidance, the maximum rate is determined on a jurisdiction-by-jurisdiction basis even if that rate exceeds the highest rate applicable to a specific award grantee. However, the classification exception would not apply to entities that do not have a statutory tax withholding obligation; for such entities, any net settlement for tax withholding would result in a liability-classified award.

In addition, an entity may change the terms of its awards related to net settlement for withholding taxes from the minimum statutory tax rate to a higher rate up to the maximum statutory tax rate. While this change may be made to existing awards, the entity would not be required to account for such a change as a modification. However, this accounting treatment applies only in these narrow circumstances (i.e., solely to change the net-settlement provisions from the minimum statutory tax rate to a higher rate up to the maximum statutory tax rate for statutory tax withholding purposes) and should not be analogized to other situations.

Practical Expedients for Nonpublic Entities

Expected-Term Practical Expedient

The ASU allows nonpublic entities to use the simplified method to estimate the expected term for awards (including liability-classified awards measured at fair value) with service or performance conditions that meet certain requirements. Such entities would apply this practical expedient as follows:

- For awards with only a service condition, nonpublic entities can estimate the expected term as the midpoint between the requisite service period and the contractual term of the award.
- For awards with a performance condition, the estimate of the expected term would depend on whether it is probable that the performance condition will be achieved:
  - If it is probable that the performance condition will be achieved, nonpublic entities can estimate the expected term as the midpoint between the requisite service period and the contractual term.
  - If it is not probable that the performance condition will be achieved, nonpublic entities can estimate the expected term as (1) the contractual term if the award does not contain an explicit service period or (2) the midpoint between the requisite service period and the contractual term if the award does contain an explicit service period.

Intrinsic Value Practical Expedient

The ASU allows nonpublic entities to make a one-time election to switch from fair value measurement to intrinsic value measurement, without demonstrating preferability, for share-based payment awards classified as liabilities.

Nonpublic entities are not allowed to make this election on an ongoing basis after the effective date of the new guidance.

Transition and Related Disclosures

The following table outlines the transition methods for an entity's adoption of ASU 2016-09:

Type	Transition Method
Recognition of excess tax benefits and tax deficiencies (accounting for income taxes)	Prospective
Unrecognized excess tax benefits (accounting for income taxes)	Modified retrospective
Classification of excess tax benefits in the statement of cash flows	Retrospective or prospective
Accounting for forfeitures	Modified retrospective
Classification and statutory tax withholding requirements	Modified retrospective
Classification of employee taxes paid in the statement of cash flows when an employer withholds shares for tax withholding purposes	Retrospective
Nonpublic entity practical expedient for expected term	Prospective
Nonpublic entity practical expedient for intrinsic value	Modified retrospective

Thinking It Through

An entity's prior-year APIC pool is not affected because prior-year excess tax benefits and tax deficiencies have already been recognized in the financial statements, and the recognition of excess tax benefits and tax deficiencies in the income statement is prospective only in the fiscal year of adoption. As a result, there is no reclassification between APIC and retained earnings in the fiscal years before adoption. The modified retrospective transition guidance for taxes only applies to previously unrecognized excess tax benefits outstanding upon adoption of ASU 2016-09 with a cumulative-effect adjustment to retained earnings.

In the period of adoption, entities are required to disclose (1) the nature of and reason for the changes in accounting principle and (2) any cumulative effects of the changes on retained earnings or other components of equity as of the date of adoption.

In addition, because the change in presentation in the statement of cash flows related to excess tax benefits can be applied either prospectively or retrospectively, entities are required to disclose (1) "that prior periods have not been adjusted" if the change is applied prospectively or (2) the "effect of the change on prior periods retrospectively adjusted" if the change is applied retrospectively. For the change in presentation in the statement of cash flows related to statutory tax withholding requirements, entities are required to disclose the "effect of the change on prior periods retrospectively adjusted."

Effective Date

For public business entities, the ASU is effective for annual reporting periods beginning after December 15, 2016, including interim periods within those annual reporting periods. For all other entities, the ASU is effective for annual reporting periods beginning after December 15, 2017, and interim periods within annual reporting periods beginning after December 15, 2018.

Early adoption will be permitted in any interim or annual period for which financial statements have not yet been issued or have not been made available for issuance. If early adoption is elected, all amendments in the ASU that apply must be adopted in the same period. In addition, if early adoption is elected in an interim period, any adjustments should be reflected as of the beginning of the annual period that includes that interim period.

Example

Entity A, an SEC registrant, adopts ASU 2016-09 in its third fiscal quarter. Entity A had $50 of excess tax benefits in each quarter in its current fiscal year to date and is not affected by adopting any of the other provisions of ASU 2016-09. In its previously issued financial statements in Form 10-Q, A recognized a total of $100 ($50 in each quarter) of excess tax benefits in APIC. In its third fiscal quarter, the period in which the ASU is adopted, A recognizes $50 of excess tax benefits in its income statement. That is, the quarter-to-date income tax provision will only include the third fiscal quarter excess tax benefits ($50). In addition, the year-to-date income tax provision will include excess tax benefits of $150 to reflect the reversal of the excess tax benefits recognized in APIC for the first two fiscal quarters ($100) and the recognition of those benefits in the income statement in those prior quarters (the $100 in excess tax benefits related to the first and second fiscal quarters are not recognized in the third quarter but are reflected on a recasted basis in the applicable prior quarters). In the quarterly information footnote of its subsequent Form 10-K filing, A will present a schedule reflecting the first and second fiscal quarters' excess tax benefits ($50 each quarter) in the income statement even though these amounts were reported in APIC in previously issued financial statements in Form 10-Q. Finally, A's financial statements in Form 10-Q issued in the year after A's adoption of the ASU will reflect the prior-year quarterly excess tax benefits (i.e., first and second fiscal quarters of the prior year) on a recasted basis in the income statement rather than in APIC.

Classification of Deferred Taxes

Background and Key Provisions

In November 2015, the FASB issued ASU 2015-17, which will require entities to present DTAs and deferred tax liabilities (DTLs) as noncurrent in a classified balance sheet. The ASU simplifies the current guidance, which requires entities to separately present DTAs and DTLs as current and noncurrent in a classified balance sheet.

The project on simplifying the balance sheet presentation of deferred taxes is part of the FASB's simplification initiative. Launched in June 2014, the simplification initiative is intended to improve U.S. GAAP by reducing costs and complexity while maintaining or enhancing the usefulness of the related financial information.

Under current guidance (ASC 740-10-45-4), entities "shall separate deferred tax liabilities and assets into a current amount and a noncurrent amount. Deferred tax liabilities and assets shall be classified as current or noncurrent based on the classification of the related asset or liability for financial reporting." Stakeholder feedback indicated that the separate presentation of deferred taxes as current or noncurrent provided little useful information to financial statement users and resulted in additional costs to preparers. Therefore, the FASB issued the ASU to simplify the presentation of deferred taxes in a classified balance sheet. Netting of DTAs and DTLs by tax jurisdiction will still be required under the new guidance.

Noncurrent balance sheet presentation of all deferred taxes eliminates the requirement to allocate a valuation allowance on a pro rata basis between gross current and noncurrent DTAs, which constituents had also identified as an issue contributing to complexity in accounting for income taxes.

Thinking It Through

The ASU will align with the current guidance in IAS 12, which requires entities to present DTAs and DTLs as noncurrent in a classified balance sheet.

The example below compares the classification of DTAs and DTLs under current U.S. GAAP with their classification under the new guidance.

Example

Company ABC has a net DTA of $100 million as of December 31, 20X1, as shown in the table below (amounts in millions):

Balance Sheet as of 12/31/X1	
	DTA/(DTL)
Inventory	$ 50
Net operating loss (NOL) carryforward	350
Fixed assets	(300)
Total DTA/(DTL)	$ 100

Company ABC expects that $100 million of the NOL carryforward will be used in the following year. Below are the current and noncurrent classifications of the DTA/(DTL) as of December 31, 20X1 (amounts in millions):

	Current U.S. GAAP		ASU 2015-17	
Description	Current	Noncurrent	Current	Noncurrent
Inventory	$ 50			$ 50
NOL carryforward	100	$ 250		350
Fixed assets		(300)		(300)
Total DTA/(DTL)	$ 150	$ (50)	$ 0	$ 100

Effective Date and Transition

The ASU requires the following:

- For public business entities, the ASU will be effective for annual periods beginning after December 15, 2016, and interim periods within those years.
- For entities other than public business entities, the ASU will be effective for annual reporting periods beginning after December 15, 2017, and interim reporting periods within annual reporting periods beginning after December 15, 2018.

The Board decided to allow all entities to early adopt the ASU for any interim or annual financial statements that have not been issued. In addition, entities are permitted to apply the amendments either prospectively or retrospectively.

In the period the ASU is adopted, an entity will need to disclose "the nature of and reason for the change in accounting principle." If the new guidance is applied prospectively, the entity should disclose that prior balance sheets were not retrospectively adjusted. However, if the new presentation is applied retrospectively, the entity will need to disclose the quantitative effects of the change on the prior balance sheets presented.

Accounting for Income Taxes: Intra-Entity Asset Transfers

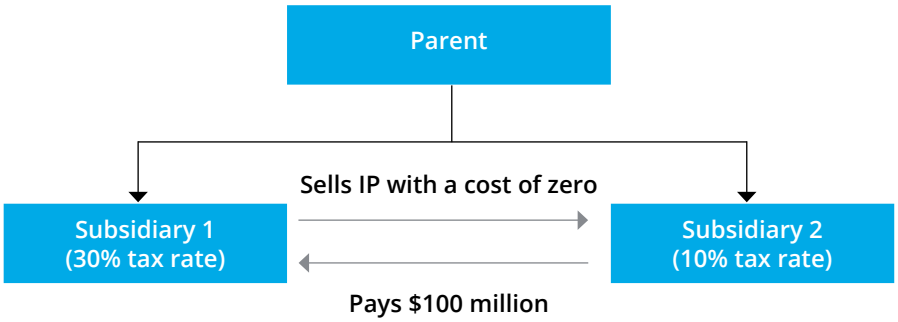
Background

In October 2016, the FASB issued ASU 2016-16, which amends the guidance in ASC 740 to remove the exception that prohibits the immediate recognition of the current and deferred tax effects of intra-entity transfers of assets. The ASU retains the exception specifically for intra-entity asset transfers of inventory. Consequently, in a manner consistent with the current requirements of ASC 740, entities are prohibited from recognizing the current and deferred tax effects of intra-entity transfers of inventory.

For intra-entity transfers of assets other than inventory, the selling (transferring) entity is required to recognize a current tax expense or benefit upon transfer of the asset. Similarly, the purchasing (receiving) entity is required to recognize a DTA or DTL, as well as the related deferred tax benefit or expense, upon receipt of the asset. The purchasing (receiving) entity measures the resulting DTA or DTL by (1) computing the difference between the tax basis of the asset in the buyer's jurisdiction and the financial reporting carrying value of the asset in the consolidated financial statements and (2) multiplying such difference by the enacted tax rate in the buyer's jurisdiction.

The example below compares the income tax accounting for intra-entity transfers of assets other than inventory before and after the ASU.

Example



Before ASU 2016-16

In the transaction above, Subsidiary 1 recognizes a gain of $100 million on the sale of intellectual property (IP) to Subsidiary 2, which is equal to the proceeds received ($100 million) less the carrying value of the IP (zero). However, in accordance with ASC 740-10-25-3(e), Subsidiary 1 is prohibited from recognizing the current tax expense associated with that $100 million gain. Therefore, upon sale, Subsidiary 1 would record the following journal entry:

Prepaid taxes	30,000,000	
Current taxes payable		30,000,000

Further, Subsidiary 2 receives a tax basis in the IP of $100 million, which is equal to the amount that it paid to Subsidiary 1. This tax basis of $100 million is greater than the carrying value of the IP in the consolidated financial statements (zero), which would generally result in a DTA. However, in accordance with ASC 740-10-25-3(e), Subsidiary 2 is prohibited from recognizing the DTA (benefit) associated with its tax-over-book basis difference. Therefore, Subsidiary 2 would not recognize any tax expense (benefit) associated with this transaction.

After ASU 2016-16

Under the ASU, the exception to recognizing current and deferred taxes on intra-entity transfers of assets is removed (unless the assets are inventory). Therefore, Subsidiary 1 is required to recognize the current tax expense associated with the gain on the sale of the IP by recording the following journal entry:

Current tax expense	30,000,000	
Current taxes payable		30,000,000

In addition, Subsidiary 2 is required to recognize the deferred tax effects associated with its purchase of the IP by recording the following journal entry:

DTA	10,000,000	
Deferred tax benefit		10,000,000

Transition Method

Entities will adopt the new guidance on a modified retrospective basis with a cumulative-effect adjustment directly to retained earnings as of the beginning of the year of adoption. Since the period of adoption is not comparable to the prior periods presented, entities will need to disclose the effects of the accounting change on the financial statements of the period of adoption.

Effective Date and Early Adoption

The guidance in the ASU is effective for public business entities for annual periods beginning on or after December 15, 2017, including interim and annual periods. For other entities, the amendments are effective for annual periods beginning after December 15, 2018, and interim periods within annual periods beginning after December 15, 2019. Early adoption is permitted for all entities as of the beginning of an annual period.

Statement of Cash Flows: Classification of Certain Cash Receipts and Cash Payments

Background

In August 2016, the FASB issued ASU 2016-15, which amends ASC 230 to add or clarify guidance on the classification of certain cash receipts and payments in the statement of cash flows. ASC 230 lacks consistent principles for evaluating the classification of cash payments and receipts in the statement of cash flows. This has led to diversity in practice and, in certain circumstances, financial statement restatements. Therefore, the FASB issued the ASU with the intent of reducing diversity in practice with respect to eight types of cash flows.

Key Provisions of the ASU

The ASU is a result of consensuses reached by the EITF on issues related to the eight types of cash flows. Key provisions of the amendments are summarized below.

Cash Flow Issues	Amendments
Debt prepayment or debt extinguishment costs	Cash payments for debt prepayment or extinguishment costs (including third-party costs, premiums paid, and other fees paid to lenders) must "be classified as cash outflows for financing activities."
Settlement of zero-coupon bonds	The cash outflows for the settlement of a zero-coupon bond must be bifurcated into operating and financing activities. The portion of the cash payment related to accreted interest should be classified in operating activities, while the portion of the cash payment related to the original proceeds (i.e., the principal) should be classified in financing activities.
Contingent consideration payments made after a business combination	Contingent consideration payments that were not made soon after a business combination (on the basis of the consummation date) must be separated and classified in operating and financing activities. Cash payments up to the amount of the contingent consideration liability recognized as of the acquisition date, including any measurement-period adjustments, should be classified in financing activities, while any excess cash payments should be classified in operating activities.

(Table continued)

Cash Flow Issues	Amendments
Proceeds from the settlement of insurance claims	Cash proceeds from the settlement of insurance claims should be classified on the basis of the nature of the loss. For insurance proceeds received in a lump-sum settlement, an entity should determine the classification on the basis of the nature of each loss included in the settlement.
Proceeds from the settlement of corporate-owned life insurance (COLI) policies and bank-owned life insurance (BOLI) policies	Cash proceeds from the settlement of COLI and BOLI polices must be classified in investing activities. However, an entity is permitted, but not required, to align the classification of premium payments on COLI and BOLI policies with the classification of COLI and BOLI proceeds (i.e., payments for premiums may be classified as investing, operating, or a combination thereof).
Distributions received from equity method investees	An entity is required to make an accounting policy election to classify distributions received from equity method investees under either of the following methods: • *Cumulative-earnings approach* — Under this approach, distributions are presumed to be returns on investment and classified as operating cash inflows. However, if the cumulative distributions received, less distributions received in prior periods that were determined to be returns of investment, exceed the entity's cumulative equity in earnings, such excess is a return of capital and should be classified as cash inflows from investing activities. • *Nature of the distribution approach* — Under this approach, each distribution is evaluated on the basis of the source of the payment and classified as either operating cash inflows or investing cash inflows. If an entity whose chosen policy is the nature of the distribution approach cannot apply the approach because it does not have enough information to determine the appropriate classification (i.e., the source of the distribution), the entity must apply the cumulative-earnings approach and report a change in accounting principle on a retrospective basis. The entity is required to disclose that a change in accounting principle has occurred as a result of the lack of available information as well as the information required under ASC 250-10-50-2, as applicable. The amendments do not address equity method investments measured under the fair value option.
Beneficial interests in securitization transactions	A transferor's beneficial interests received as proceeds from the securitization of an entity's financial assets must be disclosed as a noncash activity. Subsequent cash receipts of beneficial interests from the securitization of an entity's trade receivables must be classified as cash inflows from investing activities.

(Table continued)

Cash Flow Issues	Amendments
Separately identifiable cash flows and application of the predominance principle	The guidance provides a three-step approach for classifying cash receipts and payments that have aspects of more than one class of cash flows: 1. An entity should first apply specific guidance in U.S. GAAP, if applicable. 2. If there is no specific guidance related to the cash receipt or payment, an entity should bifurcate the cash payment or receipt into "each separately identifiable source or use [of cash] on the basis of the nature of the underlying cash flows." Each separately identifiable source or use of cash will be classified as operating, investing, or financing activities by applying the guidance in ASC 230. 3. If the cash payment or receipt cannot be bifurcated, the entire payment or receipt should be classified as operating, investing, or financing activities on the basis of the activity that is likely to be the predominant source or use of cash.

Thinking It Through

The FASB's objective in the ASU is to eliminate the diversity in practice related to the classification of certain cash receipts and payments. As a result, there could be significant changes for some entities under the revised guidance, particularly with respect to the issues discussed below.

Settlement of Zero-Coupon Bonds

The lack of guidance on the classification of payments to settle zero-coupon bonds in the statement of cash flows has led to diversity in the classification of the cash payment made by a bond issuer at the settlement of a zero-coupon bond. Some entities bifurcate the settlement payment between the principal (the amount initially received by the entity) and accreted interest. In those situations, the portion of the repayment related to principal is classified in financing activities, and the portion related to accreted interest is classified in operating activities. However, other entities do not bifurcate the settlement payment between principal and accreted interest and present the entire repayment in financing activities.

Under the ASU, entities are required to bifurcate the repayment of zero-coupon bonds into principal and accreted interest, with the principal portion classified in financing activities and the accreted interest portion classified in operating activities. As a result, entities that currently classify the entire repayment of zero-coupon bonds in financing activities will need to identify the portion of such payments that are related to accreted interest and apply the provisions of the ASU accordingly.

Distributions Received From Equity Method Investees

While ASC 230 distinguishes between returns of investment (which should be classified as inflows from investing activities) and returns on investment (which should be classified as inflows from operating activities), it does not prescribe a method for differentiating between the two. With respect to distributions from equity method investees, entities make this determination by applying a cumulative-earnings approach or a nature of the distribution approach. The ASU formalizes each of these methods and allows an entity to choose either one as an accounting policy election.

However, the ASU requires entities that choose the nature of the distribution approach to report a change in accounting principle if the information required under this approach is unavailable with respect to a particular investee. Therefore, while the ASU will not eliminate diversity in practice, entities that are currently applying the nature of the distribution approach should be mindful of the additional information and disclosure requirements under the ASU in electing a method as their accounting policy.

Beneficial Interests in Securitization Transactions

There is no specific guidance in ASC 230 on how to classify cash receipts associated with beneficial interests in securitization transactions. As a result, entities have classified the subsequent cash receipts from payments on beneficial interests obtained by the transferor in a securitization of the transferor's trade receivables as either operating activities or investing activities in the statement of cash flows. Although there is diversity in practice, we believe that entities have predominantly presented cash receipts from payments on a transferor's beneficial interests in securitized trade receivables as a cash inflow from operating activities. Accordingly, the requirement to present such cash receipts as a cash inflow from investing activities could change practice significantly.

Separately Identifiable Cash Flows and Application of the Predominance Principle

ASC 230 acknowledges that certain cash inflows and outflows may have characteristics of more than one cash flow class (e.g., financing, investing, or operating) and states that the "appropriate classification shall depend on the activity that is likely to be the predominant source of cash flows for the item." Although ASC 230 gives examples illustrating the application of the predominance principle, entities often have difficulty applying the guidance.

As a result, when cash flows have aspects of more than one cash flow class, the ASU requires that entities first determine the classification of those cash receipts and payments by applying the specific guidance in ASC 230 and other applicable ASC topics. Further, the ASU notes that "[i]n the absence of specific guidance, a reporting entity shall determine each separately identifiable source or each separately identifiable use within the cash receipts and cash payments on the basis of the nature of the underlying cash flows." The ASU goes on to observe that "[i]n situations in which cash receipts and payments have aspects of more than one class of cash flows and cannot be separated by source or use . . . the appropriate classification shall depend on the activity that is likely to be the predominant source or use of cash flows for the item." However, because the ASU does not define the term "separately identifiable" in this context, we believe that challenges may be presented related to identifying separately identifiable cash receipts and payments as well as applying the term "predominant."

Transition and Effective Date

For public business entities, the guidance is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. For all other entities, it is effective for fiscal years beginning after December 15, 2018, and interim periods within fiscal years beginning after December 15, 2019. Early adoption will be permitted for all entities.

Entities must apply the guidance retrospectively to all periods presented but may apply it prospectively if retrospective application would be impracticable.

Alternatives for Private Companies

Changes to Effective Date and Transition Guidance in Certain Private-Company ASUs

In March 2016, the FASB issued ASU 2016-03, which gives private companies a one-time unconditional option to forgo a preferability assessment the first time they elect a Private Company Council (PCC) accounting alternative within the ASU's scope. However, private companies would still be required to perform a preferability assessment in accordance with ASC 250 for any subsequent change to their accounting policy election in a manner consistent with all accounting policy changes under ASC 250.

The ASU also eliminates the effective dates of PCC accounting alternatives that are within the ASU's scope and extends the transition guidance for such alternatives indefinitely. The new guidance is effective immediately and affects all private companies within the scope of ASU 2014-02 (goodwill), ASU 2014-03 (derivatives and hedging), ASU 2014-07 (common-control leasing arrangements), and ASU 2014-18 (identifiable intangible assets). While the new standard extends the transition guidance in ASU 2014-07 (VIEs) and ASU 2014-18, it does not change the manner in which such guidance is applied. See Deloitte's March 16, 2016, *Heads Up* for more information.

Other Private-Company Matters

Throughout 2016, the PCC has discussed aspects of financial reporting that are complex and costly for private companies, including the application of VIE guidance to common-control arrangements, balance-sheet classification of debt, and liabilities and equity short-term improvements. During its April 2016 meeting, the PCC voted to recommend that the FASB add to its agenda PCC Issue 15-02, "Applying Variable Interest Entity Guidance to Entities Under Common Control."

Thinking It Through

Many entities in the industry will meet the definition of a public business entity and will therefore not be eligible for PCC alternatives. For example, a broker-dealer that is required to file financial statements with the SEC will meet the definition of a public business entity (the confidential submission of financial information to the SEC by a "material associated person" of a broker-dealer also meets the definition of a public business entity). In addition, a bank that is required to make complete U.S. GAAP financial statements publicly available under banking regulations will satisfy the first component of criterion (e) of the ASC master glossary definition of a public business entity and will need to further evaluate the second component of criterion (e) (i.e., whether its securities contain contractual restrictions on transfer). Application of the public business entity definition to banks was discussed in the Federal Financial Institutions Examination Council's September 2014 call report instructions.

On the Horizon

Financial Instruments

Hedging

In September 2016, the FASB issued a proposed ASU that would amend the hedge accounting recognition and presentation requirements of ASC 815 to (1) reduce their complexity and simplify their application by preparers and (2) improve the transparency and understandability of information conveyed to financial statement users about an entity's risk management activities by better aligning those activities with the entity's financial reporting for hedging relationships.

Although the changes proposed by the FASB are significant, constituents also should take note of those aspects of existing hedge accounting that the Board decided to retain. The proposal still would require all hedging relationships to be highly effective. Moreover, an entity would retain the ability to voluntarily dedesignate a hedging relationship, designate certain component risks of the hedged item as the hedged risk, and apply the critical-terms-match method or the shortcut method.

The FASB will determine the effective date of the proposed amendments after it considers constituent feedback; however, it has tentatively determined that earlier application of the proposed amendments will be permitted at the beginning of any fiscal year before the effective date. Comments on the proposal are due by November 22, 2016.

The sections below summarize the proposed ASU's key provisions. For additional information about the proposed ASU, see Deloitte's September 14, 2016, *Heads Up*.

Key Proposed Changes to the Hedge Accounting Model

Hedge Documentation and Qualitative Assessments of Hedge Effectiveness

Under the proposed model, an entity would be required to perform an initial prospective quantitative assessment of hedge effectiveness at hedge inception (unless the hedging relationship qualifies for application of one of the expedients that permit an assumption of perfect hedge effectiveness, such as the shortcut method or critical-terms-match method); however, the entity generally would have until its first quarterly hedge effectiveness assessment date (i.e., up to three months) to complete this quantitative assessment. All other hedge documentation still would need to be in place at hedge inception. The entity could elect to perform subsequent prospective and retrospective hedge effectiveness assessments qualitatively if certain criteria are satisfied; however, the entity could be forced to revert to quantitative assessments if, because facts and circumstances have changed, the entity may no longer assert qualitatively that the hedging relationship was and continues to be highly effective. Once an entity is forced to perform a quantitative assessment, it would be prohibited from performing qualitative assessments in future periods.

Cash Flow Hedges of Forecasted Purchases or Sales of Nonfinancial Items

For a forecasted purchase or sale of a nonfinancial item, the proposed model would permit an entity to designate the variability in cash flows attributable to changes in a contractually specified component as the hedged risk if certain criteria are satisfied. An entity could also hedge exposures arising from a contractually specified component of an agreement to purchase or sell a nonfinancial item for a period that extends beyond the contractual term or when a contract does not yet exist if the qualifying criteria will be met in a future contract and all the other cash flow hedging requirements are met.

Recognition and Presentation of the Effects of Hedging Instruments

The proposed amendments would eliminate the concept of separately recognizing periodic hedge ineffectiveness (although under the mechanics of fair value hedging, economic ineffectiveness would still be reflected in current earnings for those hedges).

For highly effective fair value hedging relationships, all changes in the fair value of the hedging instrument, including any amounts excluded from the assessment of hedge effectiveness, would be recorded in current earnings in the same income statement line as the earnings effect of the hedged item.

For highly effective cash flow hedging relationships, the change in the fair value of the hedging instrument used to assess hedge effectiveness would initially be recorded in OCI and would be reclassified out of AOCI into earnings and presented in the same income statement line as the earnings effect of the hedged item when the hedged item affects earnings. Any amounts excluded from the assessment of hedge effectiveness would be recognized immediately in earnings in the same income statement line as the earnings effect of the hedged item. Furthermore, an entity would immediately reclassify out of AOCI amounts associated with any hedged forecasted transaction whose occurrence is not probable. Such amounts would be presented in current earnings in the same income statement line in which the earnings effect of the hedged item would have been recorded had the hedged forecasted transaction occurred.

For highly effective net investment hedges, the change in the fair value of the hedging instrument used to assess hedge effectiveness would initially be recorded in the cumulative translation adjustment in OCI. When the hedged net investment affects earnings (i.e., upon a sale or liquidation), amounts would be reclassified out of the cumulative translation adjustment and be presented in the same income statement line in which the earnings effect of the net investment is presented. The portion (if any) of the hedging instrument's change in fair value that is excluded from the hedge effectiveness assessment would be recognized immediately in income (although the income statement presentation would not be prescribed).

Financial Hedging Relationships

For hedges of financial items, the proposed model (1) allows the contractually specified index rate in a variable-rate hedged item to be the designated interest rate risk, (2) retains the existing benchmark interest rate definition for fixed-rate hedged items with minor modifications to eliminate inconsistencies, and (3) designates the SIFMA Municipal Swap index as a permitted benchmark interest rate.

Fair Value Hedges of Interest Rate Risk

Under the proposal, for a fair value hedge of interest rate risk, an entity would be allowed to:

- Designate the change in only the benchmark component of total coupon cash flows attributable to changes in the benchmark interest rate as the hedged risk in a hedge of a fixed-rate financial asset or liability. However, if the current market yield of the hedged item is less than the benchmark interest rate at hedge inception (i.e., a "sub-benchmark" hedge), the entity would be required to use the total contractual coupon cash flows for its calculation.
- Consider, for prepayable financial instruments, only how changes in the benchmark interest rate affect a decision to settle a debt instrument before its scheduled maturity in calculating the change in the fair value of the hedged item attributable to interest rate risk.
- Designate as the hedged risk only a portion of the hedged item's term and measure the change in the fair value of the hedged item attributable to changes in the benchmark interest rate by "using an assumed term that begins with the first hedged cash flow and ends with the last hedged cash flow." The hedged item's assumed maturity would be the date on which the last hedged cash flow is due and payable.

Shortcut Method and Critical-Terms-Match Method

The proposal would retain both the shortcut and critical-terms-match methods and provide additional relief for entities applying those methods. It would amend the shortcut accounting requirements to allow an entity to specify, at the inception of the hedging relationship, the quantitative (long-haul) method it will use to assess hedge effectiveness and measure hedge results if it later determines that application of the shortcut method was not or no longer is appropriate. In addition, the proposal would amend certain shortcut-method criteria to allow partial-term fair value hedges to qualify for the shortcut method.

Further, the proposal would expedite an entity's ability to apply the critical-terms-match method to cash flow hedges of groups of forecasted transactions. If all other critical-terms-match criteria were satisfied, such hedges would qualify for the critical-terms-match method if all the forecasted transactions occurred within 31 days of the hedging derivative's maturity.

Disclosure Requirements

The proposed ASU would add new disclosure requirements and amend existing ones. Also, to align the disclosure requirements with the proposed changes to the hedge accounting model, the proposal would remove the requirement for entities to disclose amounts of hedge ineffectiveness. In addition, an entity would be required to provide:

- Tabular disclosure of (1) the total amounts reported in the statement of financial performance for each income and expense line item that is affected by hedging and (2) the effects of hedging on those line items.
- Disclosures about the carrying amounts and cumulative basis adjustments of items designated and qualifying as hedged items in fair value hedges.
- Qualitative disclosures describing (1) quantitative hedging goals, if any, established in developing its hedging objectives and strategies and (2) whether those goals were met.

These disclosures would be required for every annual and interim reporting period for which a statement of financial position and statement of financial performance are presented.

Adoption and Transition

Entities would adopt the proposal's provisions by applying a modified retrospective approach to existing hedging relationships as of the adoption date. After adoption, in all interim and annual periods, entities would begin to apply the new accounting and presentation model and provide the new and amended disclosures.

In each annual and interim reporting period in the fiscal year of adoption, entities would also be required to furnish certain disclosures required by ASC 250 about (1) the nature and reason for the change in accounting principle and (2) the cumulative effect of the change on the components of equity or net assets as of the date of adoption.

The proposal also describes (1) specific transition considerations related to the accounting for fair value hedges of interest rate risk, (2) one-time transition elections that allow entities to amend the documentation for existing hedging relationships and to take advantage of the guidance on qualitative assessments and the shortcut method of accounting, and (3) a one-time transition election that allows entities, for certain existing cash flow hedging relationships, to take advantage of the amendments that permit designation of a contractually specified interest rate (for variable-rate instruments) or a contractually specified component (for forecasted purchases or sales of nonfinancial items).

Liabilities and Equity — Targeted Improvements

Background

The FASB added a project to its technical agenda in 2014 to consider making targeted improvements to its guidance on the classification of financial instruments as either liabilities or equity. The objective of the project was to simplify the guidance in existing U.S. GAAP on distinguishing liabilities from equity, which involves the application of numerous complex rules and is one of the most common sources of errors and restatements.

However, the FASB tentatively decided in February 2016 to largely abandon the project after concluding that targeted improvements would not adequately address the pervasive problems related to this topic. Instead, the Board decided to seek feedback on whether it should recommence a comprehensive project on distinguishing liabilities from equity to holistically examine the associated issues. Nevertheless, the FASB issued an Invitation to Comment in August 2016 to determine whether it should undertake such a project. As a result, the Board has tentatively decided to proceed with making targeted improvements related to two narrow issues and is expected to issue a proposed ASU during the first quarter of 2017.

The tentative changes would affect the guidance in U.S. GAAP on:

- The accounting for instruments with "down-round" provisions.
- The indefinite deferral of certain pending content in ASC 480-10.

Down-Round Provisions

Background

A down-round provision is a term in an equity-linked financial instrument (e.g., a freestanding warrant contract or an equity conversion feature embedded within a host debt or equity contract) that triggers a downward adjustment to the instrument's strike price (or conversion price) if the entity issues equity shares at a lower price (or equity-linked financial instruments with a lower strike price) than the instrument's then-current strike price. The purpose of the feature is to protect the instrument's counterparty from future issuances of equity shares at a more favorable price.

Under current U.S. GAAP, a contract (or embedded equity conversion feature) that contains a down-round provision does not qualify as equity because such arrangement precludes a conclusion that the contract is indexed to the entity's own stock under ASC 815-40-15 (as illustrated in ASC 815-40-55-33 and 55-34). As a result, contracts and features that include down-round provisions do not currently qualify for the scope exception from derivative accounting in ASC 815-10 for contracts that are indexed to, and classified in, stockholders' equity. Therefore, freestanding contracts on an entity's own equity that contain a down-round feature and meet the definition of a derivative (including net settlement) are accounted for at fair value with changes in fair value recognized in earnings. Similarly, features embedded in an entity's own equity that contain down-round provisions must be separated and accounted for as derivative instruments at fair value if they meet the bifurcation criteria in ASC 815-15.

Tentative Changes

The tentative changes would apply to issuers of financial instruments (e.g., a warrant or a convertible instrument) with down-round features. Specifically excluded from the scope would be (1) freestanding financial instruments and embedded conversion options that are accounted for at fair value with changes in fair value recognized in earnings (e.g., freestanding and bifurcated embedded derivative instruments within the scope of ASC 815 and debt for which the issuer has elected the fair value option in ASC 825-10) and (2) convertible debt instruments that are separated into liability and equity components (e.g., convertible debt with beneficial conversion features or cash conversion features pursuant to ASC 470-20).

Under the tentative proposed approach, a down-round provision would not preclude an entity from concluding that the instrument or feature that includes the provision is indexed to the entity's own stock. For example, when an entity evaluates whether it is required to classify a freestanding warrant that gives the counterparty the right to acquire the entity's common stock as a liability or equity under ASC 815-40, the existence of the down-round feature would not affect the analysis. If the warrant otherwise meets the condition for equity classification, it would be classified as equity. Similarly, in the analysis of whether an embedded conversion feature in a debt host contract must be bifurcated as an embedded derivative under ASC 815-15, the existence of a down-round provision would not prevent the contract from qualifying for the scope exception in ASC 815-10-15-74 for contracts indexed to an entity's own stock and classified in stockholders' equity.

While instruments that contain down-round features would no longer be expressly precluded from equity classification, such instruments may still not qualify for equity classification for other reasons (e.g., if the issuer could be forced to net cash settle the contract). The classification of instruments as liabilities or equity would not, under the proposal, be dictated by the down-round feature. Instead, the down-round feature would affect the accounting only if it were "triggered" (i.e., the entity issued shares at a price below the strike price). Once the feature was triggered, entities would determine the value that was transferred to the holder when the price adjustment occurred.

Thinking It Through

Under current U.S. GAAP, down-round protection often results in instruments being accounted for as liabilities, with changes in fair value recorded through earnings. Under the proposed changes, fewer instruments are expected to require such classification and resulting fair value treatment. However, many instruments or embedded features are precluded from equity classification because of the existence of other terms (e.g., warrants on contingently redeemable preferred stock) and would therefore be unaffected by this proposed change.

Further, entities that present fair value financial statements (e.g., in accordance with ASC 946) would be largely unaffected by this change.

Removal of the Indefinite Deferral Under ASC 480

The transition guidance in ASC 480-10 indefinitely defers the application of some of its requirements for certain instruments and entities (i.e., certain mandatorily redeemable financial instruments of nonpublic entities that are not SEC registrants and certain mandatorily redeemable noncontrolling interests). Accordingly, such instruments may qualify as equity under U.S. GAAP even though ASC 480-10-25 suggests that they should be classified as liabilities.

ASC 480-10 requires issuers to classify mandatorily redeemable financial instruments as liabilities. Because of the indefinite deferral noted above, these requirements are labeled "pending content" in the Codification, but the transition guidance in ASC 480-10-65 provides no effective date for them. Therefore, the transition requirements under the tentative guidance would effectively provide scope exceptions for parts of the guidance in ASC 480-10 for affected entities and instruments.

Accounting for Interest Income Associated With the Purchase of Callable Debt Securities

Background and Key Provisions of the Proposed ASU

In September 2016, the FASB issued for public comment a proposed ASU that would amend the amortization period for callable debt securities purchased at a premium. The proposal would shorten the amortization period for such securities to the earliest call date.

Under current U.S. GAAP, the premium on a callable debt security is generally amortized as an adjustment of yield over the contractual life (to maturity date) of the instrument. Accordingly, there is no consideration of early payment of principal, and any unamortized premium is recorded as a loss in earnings upon the debtor's exercise of a call on a callable debt security purchased at a premium.

The FASB's proposed amendments would require the premium to be amortized to the earliest call date but would retain the accounting for the amortization of discounts on purchased callable debt securities (i.e., the discount would continue to be amortized to maturity).

Constituents have noted that under current guidance, (1) the amortization of premiums does not reflect the economics of the underlying transaction and (2) the model for pricing securities in the United States includes consideration for calls. In addition, investors generally price a security to the call date when the security is trading at a premium.

The proposed ASU states that the amendments would "more closely align the amortization period of premiums and discounts to expectations incorporated in market pricing on the underlying securities."

Effective Date and Transition

The FASB plans to determine an effective date for the final guidance after considering stakeholder feedback on the proposed ASU.

To apply the guidance, entities would use a modified retrospective approach, with the cumulative-effect adjustment recognized to retained earnings as of the beginning of the first reporting period in which the guidance is effective. Entities would also be required to provide disclosures about a change in accounting principle in the period they adopt the final standard.

Next Steps

Comments on the proposed ASU are due by November 28, 2016.

Simplifying the Balance Sheet Classification of Debt

Background

The FASB recently directed its staff to draft a proposed ASU that would simplify the classification of debt as either current or noncurrent on the balance sheet. The guidance currently in ASC 470-10 consists of an assortment of fact-specific rules and exceptions, the application of which varies according to the terms and conditions of the debt arrangement, management's expectations of when debt may be settled or refinanced, and certain post-balance-sheet events. The objective of the project is to reduce the cost and complexity of applying this guidance while maintaining or improving the usefulness of the information provided to financial statement users.

Principles-Based Approach

The FASB's tentative approach would replace the current, fact-specific guidance with a unified principle for determining the classification of a debt arrangement in a classified balance sheet as either current or noncurrent. Specifically, an entity would classify a debt arrangement as noncurrent if *either* of the following criteria is met as of the financial reporting date:[1]

- "The liability is contractually due to be settled more than 12 months (or operating cycle, if longer) after the balance sheet date."
- "The entity has a contractual right to defer settlement of the liability for at least 12 months (or operating cycle, if longer) after the balance sheet date."

As an exception to this classification principle, debt that is due to be settled within 12 months as a result of a covenant violation as of the balance sheet date would be classified as noncurrent if the debtor receives a waiver that meets certain conditions after the balance sheet date (see Covenant Violations below).

Scope

The FASB has tentatively decided to clarify that the balance sheet classification guidance in ASC 470-10 applies not only to nonconvertible debt arrangements but also to convertible debt and to mandatorily redeemable financial instruments that are classified as liabilities under ASC 480-10.

[1] Quoted text is from the FASB's summary of tentative Board decisions reached at its January 28, 2015, meeting.

Short-Term Obligations Expected to Be Refinanced on a Long-Term Basis

Under current guidance, entities that have the intent and ability to refinance a short-term obligation on a long-term basis *after* the financial reporting date — as evidenced by the post-balance-sheet-date issuance of a long-term obligation, equity securities, or a qualifying refinancing agreement — are required to present the obligation as a noncurrent liability as of the financial reporting date. The tentative approach, however, would require such short-term obligations to be classified within current liabilities because the refinancing of debt after the financial reporting date would be viewed as a new transaction that should not be retroactively reflected in the balance sheet as of that date.

Subjective Acceleration Clauses and Debt Covenants

Under existing GAAP, the classification of long-term obligations depends in part on whether they are governed by subjective acceleration clauses (SACs) for which exercise is probable (e.g., because of recurring losses or liquidity problems). Under the Board's tentative approach, however, SACs and covenants within long-term obligations would affect the classification of long-term obligations only when triggered or violated, in which case disclosure of the SAC or covenant would be required.

Thinking It Through

Under the Board's tentative approach, some liabilities that are now classified as noncurrent would be classified as current, and vice versa. For example, as a result of the proposed change to the treatment of the refinancing of short-term obligations, an entity would not be allowed to consider refinancing events after the financial reporting date but before the financial statements were issued. Thus, such debt obligations would be classified as current liabilities as of the financial reporting date. Entities should consider the timing of refinancing plans and the potential effect on the classification of short-term obligations.

Covenant Violations

Under current guidance, if the creditor can demand the repayment of a long-term obligation as of the financial reporting date because of the debtor's violation of a debt covenant, the corresponding debt obligation is classified as noncurrent if the debtor obtains a covenant waiver *before* the date the financial statements are issued and certain other conditions are met. While the Board's tentative approach would retain similar guidance, it would classify such debt as current if the waiver results in the debt's being accounted for as having been extinguished. Because debt extinguishment accounting treats the debt as a newly issued instrument, the original debt obligation, as of the balance sheet date, should be classified within current liabilities since the debtor could demand repayment as of that date.

At its October 19, 2016, meeting, the Board decided to clarify the application of the probability assessment that is associated with the waiver exception. Entities would be required to assess whether a violation of any other covenant not covered by the waiver is probable within 12 months from the reporting date. If so, the related debt would be required to be classified as current.

Presentation and Disclosure

Under the Board's tentative approach, debt that is classified as noncurrent in accordance with the exception for debt covenant waivers would be presented separately in the balance sheet. Further, as previously noted, the tentative approach would require entities to disclose information about debt covenants and SACs upon violation or trigger.

Effective Date and Transition

The Board will determine an effective date for the guidance after it considers feedback on the proposed ASU. Once finalized, the proposed approach will be applicable on a prospective basis to debt that exists as of the effective date. Early adoption will be permitted.

Next Steps

The proposed ASU is expected to be released in December 2016 or early January 2017. The comment period is expected to end no earlier than May 5, 2017.

Goodwill and Business Combinations

Subsequent Accounting for Goodwill for Public Business Entities and Not-for-Profit Entities, Including Goodwill Impairment

Background

In November 2013, the FASB endorsed (and later issued guidance on[2]) a decision by the PCC to give nonpublic business entities an accounting alternative under which they can elect to amortize goodwill and perform a simplified impairment test. The Board received feedback on the PCC accounting alternative indicating that many public business entities and not-for-profit entities had similar concerns about the cost and complexity of the annual goodwill impairment test.

In response, the Board in 2014 added to its agenda a goodwill simplification project that would be completed in two phases. The Board later separated the undertaking into two individual projects: (1) accounting for goodwill impairment and (2) subsequent accounting for goodwill for public business entities and not-for-profit entities.

Current Status and Next Steps

Under ASC 350, impairment of goodwill "is the condition that exists when the carrying amount of goodwill exceeds its implied fair value." The implied fair value of goodwill is determined in the same manner as the amount of goodwill recognized in a business combination. The process of measuring the implied fair value of goodwill is currently referred to as step 2 of the goodwill impairment test. Step 2 requires an entity to "assign the fair value of a reporting unit to all of the assets and liabilities of that unit (including any unrecognized intangible assets) as if the reporting unit had been acquired in a business combination." Consequently, the performance of step 2 of the goodwill impairment test can result in significant cost and complexity.

As part of its goodwill impairment project, the FASB issued a proposed ASU in May 2016 that would remove step 2 from the goodwill impairment test. The proposed guidance, which is intended to simplify the accounting for goodwill impairment, would require an entity to "recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit's fair value. However, that amount should not exceed the carrying amount of goodwill allocated to that reporting unit."

[2] For more information, see Deloitte's January 27, 2014, *Heads Up*.

The qualitative assessment of goodwill would be unchanged under the proposed ASU. However, all reporting units, even those with a zero or negative carrying amount, would apply the same impairment test. As noted in the proposal's Basis for Conclusions, goodwill of reporting units with a zero or negative carrying amount would not be impaired even when conditions underlying the reporting unit indicate that it was impaired. However, entities would be required to disclose any reporting units with a zero or negative carrying amount and the respective amounts of goodwill allocated to those reporting units.

Thinking It Through

The proposed guidance would significantly change the accounting for goodwill for reporting units with zero or negative carrying amounts. While current guidance addresses the assignment of liabilities to a reporting unit, practitioners have had questions about the assignment of debt. A reporting unit may have a negative carrying amount because of an entity's decision to assign debt to it, resulting in diversity in practice and different goodwill impairment outcomes.

Comments on the proposed ASU were due by July 11, 2016.[3] The FASB is redeliberating the proposed ASU and has not yet determined a proposed effective date for the final standard. A nonpublic business entity that has already elected the PCC's accounting alternative for goodwill and would like to apply the final guidance would need to perform an assessment of preferability in accordance with ASC 250.

As part of its project on the subsequent accounting for goodwill, the Board expects to consider whether to permit or require amortization of goodwill or make further changes to impairment testing methods.

Clarifying the Definition of a Business

Background

In November 2015, the FASB issued a proposed ASU related to the first phase of its project on the definition of a business. The proposal is in response to concerns that the current definition of a business has been interpreted too broadly and that many transactions are accounted for as business combinations when they are more akin to asset acquisitions. Comments on the proposed guidance were due by January 22, 2016, and were analyzed by the FASB staff at its meeting on August 24, 2016.

Under the proposal:

- To be a business, a set of assets and activities ("set") must include an input and a substantive process that together contribute to the ability to create outputs.
- If substantially all the fair value of the gross assets is concentrated in a single identifiable asset or group of similar identifiable assets, the set would not be a business.
- The definition of outputs is narrowed to be consistent with ASC 606.

Thinking It Through

The proposed guidance could affect the banking and securities industry as a result of the different accounting for business combinations and asset acquisitions. For example, acquisition costs are expensed in a business combination and capitalized in an asset acquisition. Thus, a more narrow definition of a business will result in more asset acquisitions and, therefore, more capitalized costs.

[3] See Deloitte's comment letter on the proposed ASU.

Single or Similar Asset Concentration

Under the proposal, cash and cash equivalents, DTAs, and the effects of DTLs would be excluded from an entity's assessment of gross asset concentration. If the fair value of the gross assets cannot be concentrated, the entity would apply the proposed ASU's framework for evaluating whether an input and a substantive process are both present and together contribute to the ability to produce outputs.

Thinking It Through

In the determination of gross asset concentration, neither a financial asset and a nonfinancial asset (e.g., customer deposits and customer relationships) nor different major classes of financial assets (e.g., cash, accounts receivable, and marketable securities) could be combined. Also, identifiable assets within the same major asset class that have significantly different risk characteristics could not be combined.

Input and Substantive Process Requirement

The proposal provides a framework for determining whether a set has an input and a substantive process that collectively contribute to the ability to create outputs. When a set does not yet have outputs, the set would have a substantive process only if it has an organized workforce (or an acquired contract that provides access to an organized workforce) that has the necessary skills, knowledge, or experience to perform an acquired process (or group of processes) that, when applied to an acquired input or inputs, is critical to the ability to continue producing outputs. For a set with outputs, the FASB proposed less stringent criteria for determining that the set has a substantive process. An organized workforce may represent a substantive process. However, a set may have a substantive process even without an organized workforce if an acquired process or processes contribute to the ability to continue producing outputs and cannot be replaced without significant cost, effort, or delay or are considered unique or scarce.

Definition of Outputs

Under current guidance (ASC 805-10-55-4), outputs are defined as "[t]he result of inputs and processes applied to those inputs that provide or have the ability to provide a return in the form of dividends, lower costs, or other economic benefits directly to investors or other owners, members, or participants." The proposal would change this definition to the "result of inputs and processes applied to those inputs that provide goods or services to customers, other revenues, or investment income, such as dividends or interest." The revised definition of outputs aligns the definition with the new revenue guidance in ASC 606.

Transition and Effective Date

The amendments in the proposal would be applied prospectively to any transaction that occurs on or after the effective date of the final standard. No disclosures would be required at transition. The FASB will determine the effective date and whether the proposed amendments may be applied before the effective date after it redeliberates its proposal on clarifying the scope of asset derecognition guidance and accounting for partial sales of nonfinancial assets.

For additional information, see Deloitte's December 4, 2015, *Heads Up*.

Accounting for Identifiable Intangible Assets in a Business Combination

Background

In November 2014, the FASB agreed to add to its agenda a project to explore potential changes to the guidance on accounting for identifiable intangible assets in a business combination for public business entities and not-for-profit entities. The Board will evaluate whether certain intangible assets should be subsumed into goodwill.

Current Status and Next Steps

The project is in the initial deliberations phase. At the FASB's October 28, 2015, meeting, the Board decided to conduct further research in conjunction with the IASB. The boards discussed the status of their respective projects on this topic at their June 20, 2016, meeting; however, no decisions were made.

Accounting for Partial Sales of Nonfinancial Assets

Background

In June 2016, the FASB issued a proposed ASU that would clarify the scope of the Board's recently established guidance on nonfinancial asset derecognition (ASC 610-20) as well as the accounting for partial sales of nonfinancial assets. The proposed guidance is in response to stakeholder feedback indicating that (1) the meaning of the term "in-substance nonfinancial asset" is unclear because the Board's new revenue standard does not define it and (2) the scope of the guidance on nonfinancial assets is complex and does not specify how a partial sales transaction should be accounted for or which model entities should apply. The proposed ASU would conform the derecognition guidance on nonfinancial assets with the model for revenue transactions in ASC 606. Comments on the proposed guidance were due on August 5, 2016, and the FASB is analyzing the comment letters received.

The proposed ASU would require entities to apply the guidance in ASC 610-20 to the derecognition of all nonfinancial assets and in-substance nonfinancial assets. While the concept of in-substance assets resided in ASC 360-20, this guidance would not have applied to transactions outside of real estate. The FASB is therefore proposing to add to the ASC master glossary the following definition of an in-substance nonfinancial asset:

> An asset of a reporting entity that is included in either of the following:
>
> a. A contract in which substantially all the fair value of the assets (recognized and unrecognized) promised to a counterparty is concentrated in nonfinancial assets
>
> b. A consolidated subsidiary in which substantially all the fair value of the assets (recognized and unrecognized) in the subsidiary is concentrated in nonfinancial assets.
>
> An in substance nonfinancial asset does not include:
>
> a. A group of assets or a subsidiary that is a business or nonprofit activity
>
> b. An investment of a reporting entity that is being accounted for within the scope of Topic 320 on investments — debt securities, Topic 321 on investments — equity securities, Topic 323 on investments — equity method and joint ventures, or Topic 325 on other investments regardless of whether the assets underlying the investment would be considered in substance nonfinancial assets.

Thinking It Through

The clarification that a business or nonprofit activity would not be considered an in-substance nonfinancial asset is based on another proposed ASU that would clarify and narrow the definition of a business and most likely reduce the number of real estate transactions that would be considered businesses.

Further, such transactions are likely to include significant financial assets, such as investments, hedges, deposits, and loans, and therefore would not be within the scope of the nonfinancial assets derecognition guidance in ASC 610-20.

Effective Date and Transition

The effective date of the new guidance and the transition methods would be aligned with the requirements in the new revenue standard as amended by ASU 2015-14,[4] which delays the effective date of the new revenue standard by one year and permits early adoption on a limited basis. However, an entity would be permitted to use a transition approach to adopt ASC 610-20 that is different from the one it uses to adopt ASC 606 (e.g., the entity may use the modified retrospective approach to adopt ASC 610-20 and the full retrospective approach to adopt ASC 606). If different methods are used, an entity would need to provide the transition-method disclosures required by ASC 606 and indicate the method it used to adopt ASC 610-20.

For additional information, see Deloitte's June 14, 2016, *Heads Up*.

Stock-Based Compensation and Employee Benefits

Nonemployee Share-Based Payment Accounting Improvements

Background

In December 2015, the FASB decided to add to its agenda a project on improving the accounting for nonemployee share-based payment arrangements. When the Board previously deliberated its initial share-based payment simplification project, it decided that potential improvements to the nonemployee model could involve broader changes and take longer to complete than other simplification projects. As a result, the Board concluded that reconsideration of the accounting for nonemployee share-based payments should be moved to a separate project.

Tentative Decisions

In May 2016, the FASB tentatively decided to expand the scope of ASC 718 to include all share-based payment arrangements related to acquiring both goods and services from nonemployees. The Board's tentative decision would require an entity to apply the classification and measurement guidance in ASC 718 to nonemployee share-based payments. For example, the expected term should be used to measure the fair value of stock options or similar instruments granted to nonemployees. In addition, a nonpublic entity would be permitted to use certain practical expedients, including the use of (1) calculated value to measure certain nonemployee awards and (2) intrinsic value to measure

[4] For public business entities, the standard is effective for annual reporting periods (including interim reporting periods within those periods) beginning after December 15, 2017. For nonpublic entities, the standard is effective for annual reporting periods beginning after December 15, 2018, and interim reporting periods within annual reporting periods beginning after December 15, 2019.

liability-classified nonemployee awards. Further, nonemployee share-based payments initially within the scope of ASC 718 would remain within the scope of that guidance for classification and measurement purposes (even after the nonemployee awards have vested) unless the awards are modified after performance is complete.

However, the FASB tentatively decided that attribution of any cost associated with nonemployee share-based payments would continue to be accounted for under other applicable accounting literature as though the issuer had paid cash for the goods or services.

Thinking It Through

Nonemployee share-based payments issued for goods and services are accounted for under ASC 505-50. The guidance in ASC 505-50 differs significantly from ASC 718, including the (1) determination of the measurement date, (2) accounting for performance conditions, (3) ability to use nonpublic entity practical expedients, and (4) classification of awards after vesting. The tentative decisions of this project would align such guidance.

Transition

The Board tentatively decided that a modified retrospective transition approach, with a cumulative-effect adjustment to retained earnings, would generally be required for outstanding nonemployee awards at the time of adoption. However, in allowing nonpublic companies to use calculated values to measure certain nonemployee awards, the Board tentatively decided that a prospective approach should be used for all nonemployee awards that are measured at fair value after the date of adoption.

Disclosures

With the exception of disclosures specifying the income statement effects of the change in principle in the year of adoption (or interim periods therein), the Board tentatively decided that an entity should apply the disclosure requirements in ASC 250 related to a change in accounting principle.

Finally, the Board tentatively decided that the disclosure requirements for nonemployee awards should be aligned with those in ASC 718 and that these requirements did not need to be modified.

Next Steps

The FASB staff is soliciting feedback on a draft of the proposed ASU.

Employee Benefit Plan Master Trust Reporting (EITF 16-B)

Many employee benefit plans hold investments in master trusts, in which a regulated financial institution serves as the trustee or custodian of the plan's assets as well as assets of other plans of the same employer or group of employers under common control. Because defined contribution pension plans with interests in master trusts are becoming more common, additional presentation and disclosure guidance on such trusts is needed.

In July 2016, the FASB issued a proposed ASU that seeks to improve the presentation and disclosure guidance for employee benefit plans that have investments held in master trusts. The proposed ASU addresses the following subissues related to employee benefit plan master trust reporting:

- *Presentation of master trust balances and activity on the face of the plan's financial statement* — When an employee benefit plan has investments in a master trust, the plan must disclose the balances and activity of its interest in the master trust on the face of the financial statements as well as in the footnotes. However, presentation guidance is not consistently provided within U.S. GAAP and has led to some diversity in practice in presentation of the master trust balances and activity within both the statement of net assets available for benefits and the statement changes in net assets. To eliminate this diversity, the proposed ASU requires that a plan present its total interest in master trust balances and related changes in such balances as one single line item in both the statement of net assets available for benefits and the statement charges in net assets.
- *Disclosure for plans with divided interests* — The proposed ASU requires that plans with divided interests in master trusts disclose both a list of master trust investment balances by general types of investments and the dollar amount of the individual plan's interest in each of those types of investments.
- *Disclosure of investment-related accruals* — The proposed ASU requires a plan to disclose both the investment-related other asset and liability balances for the master trust and the dollar amount of the individual plan's interest in such balances.
- *Section 401(h) account investment disclosures* — A 401(h) plan is a postretirement benefit plan that may have assets funded through the entity's defined benefit pension plan assets. The proposed ASU removes the required disclosures for Section 401(h) account assets in a health and welfare plan and instead requires the health and welfare plan to provide the name of the defined benefit pension plan with which the account asset disclosures are associated.
- *Consistency between ASC topics* — Under current U.S. GAAP, benefit plan guidance is located in ASC 960, ASC 962, and ASC 965, which contain (with the exception of ASC 965) certain guidance on master trusts. The proposed ASU aligns the guidance in these ASC topics when applicable.

The amendments in the proposed ASU would be applied retrospectively to all periods presented. Further, an entity would disclose the nature of and reason for the change in accounting principle in the first interim and annual reporting periods in which it adopts the ASU. Comments on the proposed ASU were due by September 26, 2016.

Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost

In January 2016, the FASB issued a proposed ASU on the presentation of net periodic benefit cost as part of the Board's simplification initiative. Under the proposed guidance, entities would be required to (1) disaggregate the current service cost component from the other components of net benefit cost and present it with other current compensation costs for the related employees in the income statement and (2) present the remaining components of net benefit cost elsewhere in the income statement and outside of income from operations, if such a subtotal is presented.

Further, the proposed ASU would require retrospective application for the change in the presentation of the service cost component and the other components of net benefit cost in the income statement. An entity would disclose the nature of and reason for the change in accounting principle in the first interim and annual reporting periods in which it adopts the ASU.

The FASB received more than 35 comment letters (which were due by April 25, 2016) on the proposal from various respondents, including preparers, users, professional and trade organizations, and accounting firms. At its meeting on August 24, 2016, the FASB discussed a summary of the comments received and directed its staff to perform research on particular aspects of the proposed ASU. For additional information about the proposed ASU, see Deloitte's January 28, 2016, *Heads Up*.

Restricted Cash

Background

The classification of restricted cash in the statement of cash flows, along with eight other cash-flow-related issues, was initially addressed in EITF Issue 15-F. At its November 2015 meeting, the EITF decided to address the diversity in practice related to the cash flow classification of restricted cash as a separate EITF issue. Accordingly, the FASB issued a proposed ASU on restricted cash in April 2016 and an ASU on the other eight topics in August 2016.

At its September 2016 meeting, the EITF discussed the comment letters received on the proposed ASU. On the basis of its redeliberations of the proposal, the Task Force reached a final consensus that:

- An entity should include in its cash and cash-equivalent balances in the statement of cash flows those amounts that are deemed to be restricted cash and restricted cash equivalents. The Task Force decided not to define the terms "restricted cash" and "restricted cash equivalents" but observed that an entity should continue to provide appropriate disclosures about its accounting policies pertaining to restricted cash in accordance with other GAAP. The Task Force also observed that any change in accounting policy will need to be assessed under ASC 250.
- A reconciliation between the statement of financial position and the statement of cash flows must be disclosed when the statement of financial position includes more than one line item for cash, cash equivalents, restricted cash, and restricted cash equivalents.
- An entity with a material balance of amounts generally described as restricted cash and restricted cash equivalents must disclose information about the nature of the restrictions.

For public business entities, the guidance related to the final consensus will be effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. For all other entities, it will be effective for annual periods beginning after December 15, 2018, and interim periods beginning after December 15, 2019. Early adoption of the guidance in the ASU will be permitted. A reporting entity will apply the guidance retrospectively.

The FASB ratified the final consensus at its October 5, 2016, meeting, and is expected to issue an ASU in the fourth quarter of 2016.

Disclosures by Business Entities About Government Assistance

Background and Key Provisions of the Proposed Guidance

In November 2015, the FASB issued for public comment a proposed ASU to increase transparency in financial reporting by requiring specific disclosures about government assistance received by businesses. Government assistance arrangements are legally enforceable agreements under which the government provides value to the entity (e.g., grants, loan guarantees, tax incentives). The objective of the proposed disclosure requirements is to enable financial statement users to better assess (1) the nature of the government assistance, (2) the accounting policies for the government assistance, (3) the impact of the government assistance on the financial statements, and (4) the significant terms and conditions of the government assistance arrangements.

There is no explicit guidance in current U.S. GAAP on the recognition, measurement, and disclosure of government assistance received by business entities. As a result, there is diversity in practice related to how business entities account for, and disclose information about, government assistance arrangements.

The proposed ASU would require business entities to disclose the following information about government assistance arrangements in their annual financial statements:

1. Information about the nature of the assistance, including a general description of the significant categories and the related accounting policies adopted or the method applied to account for government assistance
2. Which line items on the balance sheet and income statement are affected by government assistance and the amounts applicable to each line item
3. Significant terms and conditions of the agreement, including commitments and contingencies
4. Unless impracticable, the amount of government assistance received but not recognized directly in the financial statements. The amount of government assistance received but not recognized includes value that was received by an entity for which no amount has been recorded directly in any financial statement line item (for example, a benefit of a loan guarantee, a benefit of a below-market rate loan, or a benefit from tax or other expenses that have been abated).

Such disclosures would provide financial statement users with information about the effect of government assistance on an entity's financial results and prospects for future cash flows. In addition, the disclosures would help users better assess the nature of the assistance.

The proposed amendments would apply to entities (other than not-for-profit entities within the scope of ASC 958, employee benefit plans, and entities that have entered into government assistance agreements within the scope of ASC 740) that have entered into a "legally enforceable agreement with a government to receive value." However, such provisions would not apply to transactions in which the government is (1) "legally required to provide a nondiscretionary level of assistance to an entity simply because the entity meets applicable eligibility requirements that are broadly available without specific agreement between the entity and the government" or (2) "solely a customer" of the entity.

Effective Date and Transition

The FASB plans to determine an effective date for the final guidance after considering stakeholder feedback on the proposed ASU. To apply the guidance, entities would use a prospective approach; however, retrospective application would be allowed.

Redeliberations and Next Steps

Since the conclusion of the comment letter period on February 10, 2016, the FASB has held redeliberation sessions to discuss comments received from constituents. The tentative decisions reached through the redeliberations held on June 8, 2016, are reflected above.

The Board will continue to conduct additional redeliberations at future meetings before issuing a final ASU.

Disclosure Framework

Background

In July 2012, the FASB issued a discussion paper as part of its project to develop a framework to make financial statement disclosures "more effective, coordinated, and less redundant." The paper identifies aspects of the notes to the financial statements that need improvement and explores possible ways to improve them. The FASB subsequently decided to distinguish between the "Board's decision process" and the "entity's decision process" for evaluating disclosure requirements.

FASB's Decision Process

Overview

In March 2014, the FASB released for public comment a proposed concepts statement that would add a new chapter to the Board's conceptual framework for financial reporting. The proposal outlines a decision process to be used by the Board and its staff for determining what disclosures should be required in notes to financial statements. The FABS's objective in issuing the proposal is to improve the effectiveness of such disclosures by ensuring that reporting entities clearly communicate the information that is most important to users of financial statements. See Deloitte's March 6, 2014, *Heads Up* for additional information.

In February 2015, the Board tentatively decided that the disclosure section of each Codification subtopic (1) would state that an entity should apply materiality as described in the proposed amendments to ASC 235 in complying with the disclosure requirements and (2) would not contain language that precludes an entity from exercising discretion in determining what disclosures are necessary (e.g., "shall at a minimum provide").

In September 2015, in response to feedback from outreach activities and to maintain consistency with both current practice and the FASB's proposed ASU on the omission of immaterial disclosures (see Entity's Decision Process below for discussion of the proposed ASU), the Board issued a proposal to modify the definition of materiality in Concepts Statement 8. The proposal would replace the original discussion of materiality in Concepts Statement 8 with the U.S. Supreme Court's definition. See Deloitte's September 28, 2015, *Heads Up* for additional information.

Comments on the proposed changes to Concepts Statement 8 have been provided to the FASB.

Next Steps

The FASB will continue deliberating concerns raised in comment letters and will review feedback received as a result of its outreach activities, which included testing the Board's and entity's decision processes against various Codification topics. A final concepts statement is expected to be issued after the outreach process is complete.

Entity's Decision Process

In September 2015, to reduce entities' reluctance to omit immaterial disclosures, the FASB issued a proposed ASU that would amend the Codification to indicate that the omission of disclosures about immaterial information is not an accounting error. The proposal, which is part of the FASB's disclosure effectiveness initiative, notes that materiality is a legal concept applied to assess quantitative and qualitative disclosures individually and in the aggregate in the context of the financial statements taken as a whole. See Deloitte's September 28, 2015, *Heads Up* for additional information.

Comments on the proposed ASU have been provided to the FASB.

Topic-Specific Disclosure Reviews

In addition to proposing amendments to guidance, the FASB is analyzing ways to "further promote [entities'] appropriate use of discretion"[5] in determining proper financial statement disclosures. The Board is applying the concepts in both the entity's and the Board's decision process in considering topic-specific modifications. The FASB reached tentative decisions about disclosure requirements in the following Codification topics:

- ASC 820 (fair value measurement).
- ASC 740 (income taxes).
- ASC 715-20 (defined benefit plans).

Proposed changes to the disclosure requirements are discussed below.

Fair Value Measurement

Objective for Disclosures

In December 2015, the FASB issued for public comment a proposed ASU that would amend the requirements in ASC 820 for disclosing fair value measurements. The proposed ASU would add the following objective to ASC 820 to encourage preparers to use discretion in complying with the disclosure requirements:

> The objective of the disclosure requirements in this Subtopic is to provide users of financial statements with information about all of the following:
>
> a. The valuation techniques and inputs that a reporting entity uses to arrive at its measures of fair value, including judgments and assumptions that the entity makes
>
> b. The effects of changes in fair value on the amounts reported in financial statements
>
> c. The uncertainty in the fair value measurement of Level 3 assets and liabilities as of the reporting date
>
> d. How fair value measurements change from period to period.

[5] Quoted from "What You Need to Know About Disclosure Framework" on the FASB's Web site.

In addition, the proposed ASU would make changes (eliminations, modifications, and additions) to the fair value disclosure requirements in ASC 820, as discussed below.

Eliminated and Modified Disclosure Requirements

Policy on Timing of Transfers Between Levels and Transfers Between Levels 1 and 2

The proposed ASU would remove the requirement in ASC 820-10-50-2C for an entity to disclose its policy on the timing of transfers between levels of the fair value hierarchy. An entity would still be required to have a consistent policy on timing of such transfers. The requirement to separately disclose the amounts transferred between Level 1 and Level 2 and the corresponding reason for doing so would also be removed.

Level 3 Fair Value Measurements

The disclosure requirements for Level 3 fair value measurements would be amended as follows:

- *Valuation process* — The proposed ASU would remove requirements in ASC 820-10-50-2(f) (and related implementation guidance in ASC 820-10-55-105) for an entity to disclose its valuation processes for Level 3 fair value measurements.

Thinking It Through

Removing the disclosure requirement in ASC 820-10-50-2(f) will result in divergence between U.S. GAAP and IFRSs. The requirement was added to the FASB's and IASB's jointly issued standard on the basis of a recommendation by the IASB's expert panel. The panel explained that the disclosure would help users understand the quality of the entity's fair value estimates and give investors more confidence in management's estimate. The FASB has proposed to remove the requirement because it would conflict with the Board's proposed concepts statement. The Board indicated that disclosure of internal control procedures is outside the purpose of the notes to the financial statements and is not required under other topics in U.S. GAAP.

Removing this requirement does not change management's responsibility for internal controls over the valuation process and related auditor testing. Further, it should not affect investor confidence in the quality of the fair value estimate given the regulatory environment in the United States (e.g., SEC and PCAOB) as well as the intense scrutiny in this area. The Board also noted that investors are typically familiar with the overall valuation process.

- *Measurement uncertainty* — The proposed ASU would retain the requirement in ASC 820-10-50-2(g) to provide a narrative description of the sensitivity of the fair value measurement to changes in unobservable inputs. However, it would clarify that this disclosure is intended to communicate information about the uncertainty in measurement as of the reporting date and not to provide information about sensitivity to future changes in fair value.
- *Quantitative information about unobservable inputs* — The proposed ASU would require disclosure of the range and weighted average of the unobservable inputs to comply with the requirement in ASC 820-10-50-2(bbb) (as shown by example in the implementation guidance in ASC 820-10-55-103). Disclosing the period used to develop significant unobservable inputs based on historical data would also be required. A private company would be exempt from such a disclosure requirement.

- *Level 3 rollforward* — The proposed ASU would retain the Level 3 rollforward requirement for entities that are not private companies. For entities that are private companies, the proposed ASU would modify the Level 3 rollforward requirement and remove the requirement to disclose the change in unrealized appreciation or deprecation related to investments held as of the balance sheet date under ASC 820-10-50-2(d). Instead, disclosures would be required about transfers into and out of Level 3 and purchases (and issues) of Level 3 investments. The Board indicated that entities are already required to disclose the ending balance in the fair value hierarchy table, and they could disclose transfers into (and out of) and purchases (or issues) of Level 3 investments in a sentence rather than in a full rollforward as required today. A defined benefit plan sponsor that is a private company would also remove the reconciliation of beginning and ending balances for plan investments categorized as Level 3 within the fair value hierarchy (i.e., the Level 3 rollforward) and would be required to disclose transfers into and out of Level 3 and purchases (or issues) of Level 3 assets only in its defined benefit plan footnote (for more information about the FASB's project on reviewing defined benefit plan disclosures, see discussion below).

Thinking It Through

In its outreach on the Level 3 rollforward, the Board noted that some financial statement users believe that the rollforward is useful because it helps them understand management's decisions, especially for different economic cycles. The full rollforward was generally deemed less useful for users of private-company financial statements. Transfers into and out of Level 3 were generally considered to be the most useful aspect of the rollforward.

Net Asset Value Disclosures of Estimates of Timing of Future Events

The following disclosures currently required under ASC 820-10-50-6A(b) and ASC 820-10-50-6A(e) would apply only when they have been communicated to the reporting entity by the investee or are otherwise made publicly available (even if not specifically communicated to the investor):

- "For each class of investment that includes investments that can never be redeemed with the investees, but the reporting entity receives distributions through the liquidation of the underlying assets of the investees, the reporting entity's estimate of the period of time over which the underlying assets are expected to be liquidated by the investees."
- "[W]hen the restriction from redemption might lapse."

If the timing is unknown, the entity would be required to disclose that fact.

Thinking It Through

The objective of this change is to prevent an investor from having to make its own estimate when it does not have knowledge of the timing from the investee or other public source. In addition, ASU 2015-07 removed the requirement for entities to categorize within the levels of the fair value hierarchy all investments they have measured under the net asset value practical expedient.

New Disclosure Requirements — Unrealized Gains and Losses

Entities that are not private companies would disclose fair value changes for assets and liabilities held as of the balance sheet date disaggregated by fair value hierarchy level (i.e., Levels 1, 2, and 3) for (1) net income before taxes and (2) comprehensive income. This is currently required only for the Level 3 amounts within net income under ASC 820-10-50-2(c) and (d). This requirement would not apply to private companies in accordance with the private-company decision-making framework.

Transition and Next Steps

The proposed ASU requires that the modifications to disclosures about changes in unrealized gains and losses and the changes in the quantitative information about unobservable inputs (see discussion above) would be applied prospectively beginning in the period of adoption. Entities would apply all other changes in disclosures retrospectively to all periods presented.

The FASB did not propose an effective date. Rather, the Board indicated that it plans to determine such date after considering stakeholders' feedback on the proposed guidance.

Comments on the proposed ASU were due by February 29, 2016, and were discussed at the FASB's meeting on June 1, 2016, at which it was decided that additional outreach would be conducted with investors and other financial statement users. It is not currently expected that a final ASU will be issued in 2016.

Income Taxes

Background

In July 2016, the FASB issued a proposed ASU that would modify or eliminate certain disclosure requirements related to income taxes as well as establish new requirements. The proposed ASU is the result of the application of the Board's March 2014 proposed concepts statement to disclosures about income taxes. Comments on the proposed ASU were due by September 30, 2016.

Key Provisions of the Proposed ASU

Scope

Although many of the amendments would apply to all entities that are subject to income taxes, certain amendments would apply only to public business entities.

As part of the proposal, the FASB decided that it would also replace the term "public entity," as defined in the glossary in ASC 740-10, with "public business entity," as defined in the ASC master glossary. The definition of a public business entity includes certain types of entities that the definition of a public entity under ASC 740 does not include. Thus, the disclosure requirements in ASC 740 that currently apply only to public entities would apply to other entities as well.

Indefinitely Reinvested Foreign Earnings

The proposed ASU would require all entities to explain any change to an indefinite reinvestment assertion made during the year, including the circumstances that caused such change in assertion. All entities would also be required to disclose the amount of earnings for which there was a change in assertion made during the year. In addition, all entities would be required to disclose the aggregate of cash, cash equivalents, and marketable securities held by their foreign subsidiaries.

Such information is intended to give financial statement users information that will help them predict the likelihood of future repatriations and the associated income tax consequences related to foreign indefinitely reinvested earnings.

Unrecognized Tax Benefits

The proposed ASU would modify the disclosure requirements for a public business entity related to unrecognized tax benefits. It would also add a requirement for entities to disclose, in the tabular reconciliation of the total amount of unrecognized tax benefits required by ASC 740-10-50-15A(a), settlements disaggregated by those that have been (or will be) settled in cash and those that have been (or will be) settled by using existing DTAs (e.g., settlement by using existing net operating loss or tax credit carryforwards).

A public business entity would also be required to provide a breakdown (i.e., a mapping) of the amount of total unrecognized tax benefits shown in the tabular reconciliation by the respective balance-sheet lines on which such unrecognized tax benefits are recorded. If an unrecognized tax benefit is not included in a balance-sheet line, such amount would be disclosed separately. In addition, a public business entity would be required to disclose the total amount of unrecognized tax benefits that are offset against existing DTAs for net operating loss and tax credit carryforwards.

Under the guidance currently in ASC 740-10-50-15(d), all entities must disclose details of tax positions for which it is reasonably possible that the total amount of unrecognized tax benefits will significantly increase or decrease in the next 12 months. The proposed ASU would eliminate this disclosure requirement.

Further, the proposed ASU would amend the example in ASC 740-10-55-217 to illustrate the applicability of the proposed disclosure requirements related to unrecognized tax benefits.

Operating Loss and Tax Credit Carryforwards

Currently, entities are required to disclose the amount and expiration dates of operating losses and tax credit carryforwards for tax purposes. Historically, there has been diversity in practice related to this disclosure requirement. The proposed ASU would reduce this diversity by requiring a public business entity to disclose the total amount of:

- Federal, state, and foreign gross net operating loss and tax credit carryforwards (i.e., not tax effected) by period of expiration for each of the first five years after the reporting date and a total for any remaining years.
- Federal, state, and foreign DTAs related to net operating loss and tax credit carryforwards (i.e., tax effected) before any valuation allowance.

Thinking It Through

Generally, an entity should measure a DTA in accordance with the recognition and measurement criteria in ASC 740. While the proposed ASU uses the term “deferred tax asset,” it is unclear whether that term as used in the proposal refers to a DTA measured under the ASC 740 criteria or simply the tax-effected amount of the net operating loss and tax credit carryforwards as reflected on the income tax returns as filed.

As discussed previously, a public business entity would also be required to disclose the total amount of unrecognized tax benefits that are offset against existing DTAs for net operating loss and tax credit carryforwards.

In addition, the proposed ASU would modify the disclosure requirement related to net operating loss and tax credit carryforwards for entities other than public business entities. An entity other than a public business entity would be required to disclose the total gross amounts of federal, state, and foreign net

operating loss and tax credit carryforwards (i.e., not tax effected) along with their expiration dates. The example in ASC 740-10-55-218 through 55-222 (as amended) would illustrate the applicability of these disclosure requirements.

Rate Reconciliation

ASC 740-10-50-12 currently requires a public business entity to disclose a reconciliation of the reported amount of income tax expense (or benefit) from continuing operations to the amount of income tax expense (or benefit) that would result from multiplying the pretax income (or loss) from continuing operations by the domestic federal statutory tax rate. The proposed ASU would amend the requirement for a public business entity to disclose the income tax rate reconciliation in a manner consistent with SEC Regulation S-X, Rule 4-08(h).

As amended, ASC 740-10-50-12 would continue to require a public business entity to disclose a reconciliation of the reported amount of income tax expense (or benefit) from continuing operations to the amount of income tax expense (or benefit) that would result from multiplying the pretax income (or loss) from continuing operations by the domestic federal statutory tax rate. However, the amendment would modify the requirement to disaggregate and separately present components in the rate reconciliation that are greater than or equal to 5 percent of the tax at the statutory rate in a manner consistent with the requirement in Rule 4-08(h).

Government Assistance

As a result of deliberations on its November 2015 proposed ASU on government assistance, the FASB decided to require an entity to disclose certain information related to assistance received from a governmental unit that reduces the entity's income taxes. Accordingly, the proposed ASU on income tax disclosures would require all entities that receive income tax-related government assistance to disclose a "description of a legally enforceable agreement with a government, including the duration of the agreement and the commitments made with the government under that agreement and the amount of benefit that reduces, or may reduce, its income tax burden." This disclosure requirement would apply only when the government determined whether, under such agreement, the entity would receive assistance and, if so, how much it would receive even if it met the applicable eligibility requirements. In the absence of a specific agreement between the entity and the government, the entity would not be required to disclose this information if the entity obtained the government assistance because it met eligibility requirements that apply to all taxpayers.

Other Income Tax Disclosure Requirements

The proposed ASU would require all entities to disclose the following:

- The amount of pretax income (or loss) from continuing operations disaggregated by foreign and domestic amounts.
- The amount of income tax expense (or benefit) from continuing operations disaggregated by foreign and domestic amounts.
- The amount of income taxes paid disaggregated by foreign and domestic amounts. A further disaggregation would be required for any country that is significant to the total amount of income taxes paid.
- An enacted tax law change if it is probable that such change would have an effect on the entity in the future.

In the determination of pretax income (or loss), foreign income tax expense (or benefit), or foreign income taxes paid, "foreign" refers to any country outside the reporting entity's home country.

In addition, the proposal would require public business entities to explain any valuation allowance recognized or released during the year along with the corresponding amount.

The proposed ASU is also aligned with the guidance in the proposed ASU on assessing the materiality of disclosures, which allows an entity to consider materiality when assessing income tax disclosure requirements.

Transition Guidance and Effective Date

The proposed ASU's amendments would be applied prospectively. The FASB will determine an effective date for the final guidance after it has considered feedback from stakeholders.

Defined Benefit Plans

In January 2016, the FASB issued a proposed ASU that would modify the disclosure requirements for employers that sponsor defined benefit pension or other postretirement plans. The proposed ASU contains an overall objective for the disclosures and guidance on how an entity would consider materiality in determining the extent of its defined benefit plan disclosures. The proposed ASU would add to or remove from ASC 715 a number of disclosure requirements related to an entity's defined benefit pension and other postretirement plans. The Board believes that additional costs incurred by entities as a result of implementing the proposed new disclosure requirements would be offset by cost reductions associated with the elimination of other disclosure requirements as well as the omission of immaterial disclosures.

The amendments in the proposed ASU would be applied retrospectively to all periods presented, except for those related to disclosures about plan assets that entities measure by using the net asset value practical expedient. Such changes would be applied beginning with the initial period of adoption.

The FASB received more than 30 comment letters (which were due by April 25, 2016) on the proposal from various respondents, including preparers, professional and trade organizations, and accounting firms. At its meeting on July 13, 2016, the FASB discussed a summary of the comments received and directed its staff to perform research on particular aspects of the proposed ASU. For additional information about the proposed ASU, see Deloitte's January 28, 2016, *Heads Up*.

Other Topics

Banking and Securities Regulatory Updates

OCC Updates Bank Accounting Advisory Series

In August 2016, the OCC issued the annual update to its Bank Accounting Advisory Series, which "expresses the office's views on accounting topics relevant to national banks and federal savings associations." Topics addressed in the update include acquired loans, allowances for loans and lease losses, other real estate owned, and other borrowings.

For more information, see the press release on the OCC's Web site.

SEC Approves SIPC Series 600 Rules

In March 2016, the SEC issued a final rule approving the SIPC Series 600 rules, which prescribe the form and content of the independent accountant's report on applying agreed-upon procedures to Form SIPC-7 or Form SIPC-3 (the "AUP report") filed in accordance with Rule 17a-5(e)(4) of the Exchange Act. While the SIPC Series 600 rules do not eliminate the requirement for a broker-dealer to file an AUP report, they provide that a broker-dealer is only required to file this report (and Form SIPC-7 or Form SIPC-3) with the SIPC (i.e., a broker-dealer is no longer required to file such documentation with its designated examining authority (e.g., FINRA) or the SEC). Minor changes have been made to the report template to make reference to the SIPC Series 600 rules. The SIPC Series 600 rules are effective for all broker-dealers for fiscal years ending on or after April 30, 2016.

For more information, see the Rule 600 Reports page on the SIPC's Web site.

SEC and AICPA Updates

Background

The SEC continues to focus on rulemaking, particularly in connection with its efforts to complete mandated actions under the Dodd-Frank Act and to implement provisions under the FAST Act. Key SEC rulemaking activities and other developments that have occurred since the last edition of this publication are discussed below.

Non-GAAP Measures

Press coverage and SEC scrutiny of non-GAAP measures have resulted from the Commission's concerns about (1) the increased use and prominence of such measures, (2) their potential to be misleading, and (3) the progressively larger difference between the amounts reported for them and for GAAP measures. In a speech on June 27, 2016, SEC Chair Mary Jo White reiterated the SEC's concerns about practices that can result in misleading non-GAAP disclosures. She exhorted companies "to carefully consider [SEC guidance on this topic] and revisit their approach to non-GAAP disclosures." She also urged "that appropriate controls be considered and that audit committees carefully oversee their company's use of non-GAAP measures and disclosures."

In May 2016, the SEC staff issued new and updated Compliance and Disclosure Interpretations (C&DIs) that clarify the SEC's guidance on non-GAAP measures. The updated guidance was intended to change certain practices about which the SEC has expressed concern. In remarks after the issuance of the C&DIs, the SEC staff strongly encouraged registrants to "self-correct" before the staff considers any further rulemaking or enforcement action related to non-GAAP measures.

For more information, see Deloitte's *A Roadmap to Non-GAAP Financial Measures*.

Thinking It Through

For the 12 months ended July 31, 2016, non-GAAP measures ranked second in the top-ten list of topics frequently commented on by the SEC's Division of Corporation Finance (the "Division") as part of its filing review process, moving up from fourth place for the comparable prior year. Over the next year, we expect the number of SEC comments to continue to remain high and even increase until the guidance in the updated C&DIs has been fully incorporated into practice. The SEC staff's most recent comment letters have particularly focused on the use and prominence of non-GAAP measures in press releases. Comments on press releases and filed documents have also centered on disclosures, including reconciliation requirements and the purpose and use of such measures. In addition, we expect to see more comments about the use of misleading measures, including measures that use individually tailored accounting principles, and the tax effect of non-GAAP adjustments. For more information about SEC comment letter trends, see Deloitte's *SEC Comment Letters — Including Industry Insights: What "Edgar" Told Us* and the 2016 supplement, *SEC Comment Letters — Statistics According to "Edgar."*

SEC Adopts Rules to Modernize Information Reported by Funds, Require Liquidity Risk Management Programs, and Permit Swing Pricing

In October 2016, the SEC voted to adopt changes to modernize and enhance the reporting and disclosure of information by registered investment companies and to enhance liquidity risk management by open-end funds, including mutual funds and exchange traded funds. The new rules will enhance the quality of information available to investors and will allow the SEC to more effectively collect and use data reported by funds. The rules will also promote effective liquidity risk management across the open-end-fund industry and will enhance disclosure regarding fund liquidity and redemption practices. The new rules permit the use of "swing pricing" by certain open-end management investment companies.

The changes are part of the Commission's initiative to enhance its monitoring and regulation of the asset management industry.

For more information, see the press release on the SEC's Web site.

SEC Issues Rules for Securities Clearing Agencies

In September 2016, the SEC issued a final rule and a proposed rule related to covered clearing agencies.

The final rule establishes "enhanced standards for the operation and governance" of covered clearing agencies. The final rule's scope includes "SEC-registered securities clearing agencies that have been designated as systemically important by the Financial Stability Oversight Council . . . or that are involved in more complex transactions." Such clearing agencies "will be subject to new requirements regarding, among other things, their financial risk management, governance, recovery planning, operations, and disclosures to market participants and the public."

Under the proposed rule, a covered clearing agency would be defined as "any registered clearing agency that provides the services of a central counterparty, central securities depository, or a securities settlement system." The proposal would also define various terms related to covered clearing agencies.

For more information, see the press release on the SEC's Web site.

SEC Reminds Registrants of Best Practices for Implementing New Revenue, Lease, and Credit Loss Accounting Standards

In recent speeches, the SEC staff has reminded registrants about best practices to follow in the periods leading up to the adoption of ASU 2014-09 (on revenue), ASU 2016-02 (on leases), and ASU 2016-13 (on credit losses). The staff's comments, which reiterated themes the Commission has addressed over the past year, focused on internal control over financial reporting (ICFR), auditor independence, and disclosures related to implementation activities.

For more information, see Deloitte's September 22, 2016, *Financial Reporting Alert*.

SEC Proposes to Shorten Standard Settlement Cycle for Broker-Dealer Securities Transactions

In September 2016, the SEC issued a proposed rule that would "shorten the standard settlement cycle for most broker-dealer transactions from three business days after the trade date ('T+3') to two business days after the trade date ('T+2')." The purpose of the proposed amendments is "to reduce a number of risks, including credit risk, market risk, and liquidity risk and, as a result, reduce systemic risk for U.S. market participants."

For more information, see the press release on the SEC's Web site.

SEC Publishes Final Rule on Cross-Border Security-Based Swaps

In February 2016, the SEC issued a final rule related to cross-border security-based swaps (SBSs). Under the final rule, which is being issued in response to a mandate of the Dodd-Frank Act, "a non-U.S. company that uses personnel located in a U.S. branch or office to arrange, negotiate, or execute a security-based swap transaction in connection with its dealing activity [must] include that transaction in determining whether it is required to register as a security-based swap dealer."

For more information, see the press release on the SEC's Web site.

SEC Publishes Final Rules on SBSs

In April 2016, the SEC issued final rules on SBSs that "implement provisions of Title VII relating to business conduct standards and the designation of a chief compliance officer for [SBS] dealers and major [SBS] participants." In addition, the rules address "the cross-border application of the rules and the availability of substituted compliance." The final rules, which became effective on July 12, 2016, include:

- *Rule 15Fh-1* — Defines the scope of the rules.
- *Rule 15Fh-2* — Defines terms used throughout the rules.
- *Rule 15Fh-3* — Addresses the business conduct requirements applicable to SBS entities.

- *Rule 15Fh-4* — Outlines unlawful activities for SBS entities and contains requirements for SBS dealers that advise special entities.
- *Rule 15Fh-5* — Provides requirements for SBS entities that act as counterparties to special entities.
- *Rule 15Fh-6* — Imposes pay-to-play restrictions on SBS dealers.
- *Rule 15k-1* — Outlines requirements for chief compliance officers.

For more information, see the speech by SEC Chair Mary Jo White on the SEC's Web site.

SEC Issues Final Rule to Establish Trade Acknowledgment and Verification Requirements for SBS Transactions

In June 2016, the SEC issued a final rule to establish trade acknowledgment and verification requirements for SBS transactions. Under the final rule, which is being issued in response to a mandate of the Dodd-Frank Act, an SBS entity that enters into an SBS transaction is required to do the following:

- "Provide a trade acknowledgment electronically to its transaction counterparty promptly, and no later than the end of the first business day following the day of execution."
- "Promptly verify or dispute with its counterparty the terms of a trade acknowledgment it receives."
- "Have written policies and procedures in place that are reasonably designed to obtain verification of the terms outlined in any trade acknowledgment that it provides."

In addition, certain broker-dealers that are SBS entities will be exempt from the requirements in Exchange Act Rule 10b-10 if they meet the requirements of the final rule. The final rule became effective on August 16, 2016.

For more information, the press release on the SEC's Web site.

SEC Issues Final Rule on Regulation SBSR

In July 2016, the SEC issued a final rule that amends Regulation SBSR on the reporting and dissemination of SBS information. The purpose of the final rule, which implements requirements in Title VII of the Dodd-Frank Act, is to "increase transparency in the security-based swap market." The final rule became effective on October 11, 2016.

For more information, see the press release on the SEC's Web site.

SEC Issues Final Rule Granting Regulatory Access to Data Held by SBS Data Repositories

In August 2016, the SEC issued a final rule that amends Rule 13n-4 of the Exchange Act to give certain regulators and other authorities access to SBS data repositories. Specifically, the final rule:

- Requires "either a memorandum of understanding or other arrangement between the Commission and the recipient of the data to address the confidentiality of the security-based swap data provided to the recipient."
- Identifies "the five prudential regulators named in the statute, as well as the Federal Reserve banks and the Office of Financial Research, as being eligible to access data."

- Addresses "factors that the Commission may consider in determining whether to permit other entities to access data."

For more information, see the press release on the SEC's Web site.

SEC Issues Proposed and Final Rules Related to Investment Advisers

In June 2016, the SEC issued a proposed rule that would require "SEC-registered investment advisers to adopt and implement written business continuity and transition plans reasonably designed to address operational and other risks related to a significant disruption in the investment adviser's operations." Further, such advisers would need to "make and keep all business continuity and transition plans that are currently in effect or at any time within the past five years were in effect."

In August 2016, the SEC issued a final rule (effective October 31, 2016) to improve the reporting and disclosure requirements for investment advisers. Specifically, the final rule amends:

- Form ADV to (1) require investment advisers to disclose additional information (e.g., about their "separately managed account business"), (2) include an approach under which "private fund adviser entities operating a single advisory business" can use a single Form ADV to register, and (3) make certain technical corrections to "Form ADV items and instructions."
- Investment Advisers Act rules to (1) require advisers to maintain additional records of performance-related calculations and communications and (2) "remove transition provisions that are no longer necessary."

Advisers will need to begin complying with the amendments on October 1, 2017.

For more information on the proposed rule, see the press release on the SEC's Web site.

For more information on the final rule, see the press release on the SEC's Web site.

SEC Requests Comments on Regulation S-K

In April 2016, the SEC issued a concept release that seeks feedback from constituents on modernizing certain business and financial disclosure requirements of Regulation S-K. The main requirements of Regulation S-K, which is the central repository for nonfinancial statement disclosure requirements for public companies, were established more than 30 years ago, and the modernization and optimization of these requirements may be called for as a result of evolving business models, new technology, and changing investor interests.

The release is part of the SEC's ongoing disclosure effectiveness initiative, which is a broad-based review of the Commission's disclosure, presentation, and delivery requirements for public companies. It follows the SEC's issuance last fall of a request for comment that sought feedback on the effectiveness of financial disclosure requirements in Regulation S-X that apply to certain entities other than the registrant.

For more information, see Deloitte's April 18, 2016, *Heads Up*.

SEC Requests Comments on Certain Regulation S-K Disclosure Requirements

In August 2016, the SEC published a request for comment (with an October 31, 2016, comment deadline) as part of its disclosure effectiveness initiative. The request for comment seeks feedback on certain disclosure requirements in Subpart 400 of Regulation S-K related to management, certain security holders, and corporate governance matters. The Commission plans to take the comments received into account when it develops its study on Regulation S-K, which is required by the FAST Act.

For more information, see the press release on the SEC's Web site.

SEC Proposes to Eliminate Outdated and Duplicative Disclosure Requirements

In July 2016, the SEC issued a proposed rule that would amend certain of the Commission's disclosure requirements that may be redundant, duplicative, or outdated, or may overlap with other SEC, U.S. GAAP, or IFRS disclosure requirements. The proposal also seeks comment on whether certain of the SEC's disclosure requirements that overlap with requirements under U.S. GAAP should be retained, modified, eliminated, or referred to the FASB for potential incorporation into U.S. GAAP.

The proposed amendments are the next step in the SEC's ongoing disclosure effectiveness initiative. As part of the initiative, the SEC in April 2016 also issued a concept release that sought feedback on modernizing certain business and financial disclosure requirements of Regulation S-K.

Thinking It Through

The implications of the proposal are likely to vary depending on the category of change (e.g., duplicate, overlapping, superseded). The effect of some changes may not be significant if their purpose is only to eliminate a duplicated or superseded requirement. Changes to address overlapping requirements could have a more significant effect since they can result in what the SEC describes as (1) disclosure location considerations and (2) bright-line threshold considerations.

For more information, see Deloitte's July 18, 2016, *Heads Up* and the press release on the SEC's Web site.

SEC Staff Updates C&DIs Related to Regulation S-K, the Securities Act, and Other Topics

In October 2016, the staff in Division staff updated C&DIs related to Regulation S-K, Item 402(u), and added the following new questions:

- *Question 128C.01* — Clarifies what type of consistently applied compensation measure (CACM) a registrant should select to identify the median employee when a registrant does not use annual total compensation calculated in accordance with Regulation S-K, Item 402(c)(2)(x).
- *Question 128C.02* — Clarifies whether a registrant may use hourly or annual rates of pay in determining its CACM.
- *Question 128C.03* — Clarifies the time period a registrant may use when it uses a CACM to identify the median employee.

- *Question 128C.04* — Clarifies the treatment of furloughed employees by registrants in the identification of the median employee.
- *Question 128C.05* — Clarifies the circumstances under which a worker is considered an independent contractor or a leased worker.

In September 2016, the Division staff issued the following C&DIs:

- *Question 139.33 and Question 126.41 related to Securities Act sections and forms* — Include guidance on self-directed "brokerage windows."
- *Question 301.03 related to Regulation AB* — Clarifies whether a funding-agreement-backed note with certain characteristics should be considered an "asset-backed security," as that term is defined in either Item 1101(c) of Regulation AB or Section 3(a)(79) of the Exchange Act.

In July 2016, the Division issued the following C&DIs:

- *Question 103.11 related to filing Schedules 13D and 13G (Rule 13d-1)* — Addresses whether a shareholder is exempt from filing Schedule 13G on the basis of the provisions in the Hart-Scott-Rodino Act.
- *Question 111.02 and Question 125.13 related to Securities Act sections and forms* — Contain questions related to an issuer's representation about the absence of a distribution of the securities received in an exchange.
- *Question 140.02 related to Regulation S-K* — Discusses how, in situations in which "a selling security holder is not a natural person," a registrant should "satisfy the obligation in Item 507 of Regulation S-K to disclose the nature of any position, office, or other material relationship that the selling security holder has had within the past three years with the registrant or any of its predecessors or affiliates."

In June 2016, the Division updated Section 271 of its C&DIs on rules related to the Securities Act. The updated guidance addresses questions about the completion of a merger transaction.

SEC Proposes Amendments to Broker-Dealers' Disclosures About Order Handling Information

In July 2016, the SEC issued a proposed rule that would enhance the requirements related to broker-dealers' disclosures about order handling information. Specifically, the proposal would require broker-dealers to "disclose the handling of institutional orders to customers" and to include additional information in their existing retail order disclosures.

For more information, see the press release on the SEC's Web site.

SEC Proposes Amendments to Definition of Smaller Reporting Company

In June 2016, the SEC issued a proposed rule that "would expand the number of companies that qualify as smaller reporting companies, thus qualifying for certain existing scaled disclosures provided in Regulation S-K and Regulation S-X." Specifically, the proposal would increase the qualification threshold from less than $75 million of public float to less than $250 million. Further, companies without a public float "would be permitted to provide scaled disclosures if [their] annual revenues are less than $100 million, as compared to the current threshold of less than $50 million in annual revenues."

For more information, see Deloitte's June 29, 2016, journal entry and the press release on the SEC's Web site.

Thinking It Through

The proposal does not change the $75 million public float threshold in the SEC's definition of "accelerated filer." Therefore, a company could qualify as a smaller reporting company and be eligible for the scaled disclosures but may also be an accelerated filer and subject to those requirements, including the shorter deadlines for periodic filings and the requirement to include an auditor's attestation report on ICFR.

FAST Act Amends JOBS Act and SEC Disclosure Requirements

The FAST Act became law in December 2015. Among its many provisions, it amends the JOBS Act and certain SEC disclosure requirements as well as establishes a new statutory exemption for private resales of securities. Specific provisions of the FAST Act include those related to JOBS Act changes for IPOs of emerging growth companies (EGCs), Form 10-K and Regulation S-K disclosure changes, a new Section 4(a)(7) exemption for private resales, incorporation by reference for smaller reporting companies, and an amendment to registration thresholds applicable to savings and loan holding companies.

For more information, see Deloitte's December 8, 2015, journal entry as well as the announcement on the SEC's Web site.

Thinking It Through

The aim of this legislation is make it easier for EGCs to gain exposure to the capital markets to access funding by easing regulations related to when an EGC can begin its road show as well as the omission of certain historical financial information to the extent that such information is not expected to be required at the time of an IPO's effectiveness.

SEC Releases Guidance Related to FAST Act

In January 2016, the SEC issued interim final rules and form amendments to implement certain provisions of the FAST Act. Among other aspects, the rules revise Forms S-1 and F-1 to permit an EGC to omit financial information from registration statements filed before an IPO (or confidentially submitted to the SEC for review) for historical periods required by Regulation S-X if the EGC reasonably believes that it will not be required to include these historical periods at the time of the contemplated offering. The rules and amendments became effective on January 19, 2016.

In addition, in December 2015, the SEC issued a number of C&DIs related to the FAST Act. Topics addressed in the C&DIs include (1) whether, and in what circumstances, an EGC can omit interim financial statements or financial statements of other entities from its registration statement and (2) FAST Act requirements that affect savings and loan companies.

See Deloitte's December 8, 2015, journal entry for more information about the FAST Act's effects on securities laws and regulations. Also see Deloitte's January 15, 2016, journal entry for further details on the interim final rules and January 12, 2016, and December 18, 2015, journal entries for more information about the C&DIs.

SEC Adopts Rules to Implement FAST Act and JOBS Act Provisions

In May 2016, the SEC issued a final rule that (1) marks the completion of the Commission's rulemaking mandates under the JOBS Act and (2) implements provisions of the FAST Act. Specifically, the final rule:

- Amends "Exchange Act Rules 12g-1 through 12g-4 and 12h-3 which govern the procedures relating to registration and termination of registration under Section 12(g), and suspension of reporting obligations under Section 15(d), to reflect the new thresholds established by the JOBS Act and the FAST Act."
- Applies "the definition of 'accredited investor' in Securities Act Rule 501(a) to determinations as to which record holders are accredited investors for purposes of Exchange Act Section 12(g)(1)." The final rule also revises the definition of "held of record" and establishes a nonexclusive safe harbor under Exchange Act Section 12(g).

The final rule became effective on June 9, 2016. For more information, see the press release on the SEC's Web site.

In June 2016, the SEC issued an interim final rule that implements provisions mandated by the FAST Act. The interim final rule allows Form 10-K filers to provide a summary of business and financial information contained in the annual report. The rule indicates that "a registrant may, at its option, include a summary in its Form 10-K provided that each item in the summary includes a cross-reference by hyperlink to the material contained in the registrant's Form 10-K to which such item relates." In addition, the rule solicits comments on whether it should (1) include specific requirements or guidance related to the form and content of the summary and (2) be expanded to include other annual reporting forms. The interim final rule became effective on June 9, 2016.

For more information on the interim final rule, see Deloitte's June 2, 2016, journal entry and the press release on the SEC's Web site.

Thinking It Through

The SEC considered the interim final rule's effects on registrants and noted that the rule was not likely to significantly alter their current disclosure practices. SEC rules do not currently prohibit registrants from voluntarily including a summary in their Form 10-K; however, on the basis of the SEC staff's review of select Form 10-K filings, most do not include such a summary. Instead, the vast majority of registrants include a fully hyperlinked table of contents that allows users to easily navigate to corresponding disclosure items.

SEC and Other Organizations Propose Guidance on Incentive-Based Compensation Arrangements

In May 2016, the SEC and several other government agencies, including the Federal Reserve Board, OCC, FDIC, FHFA, and NCUA, jointly issued a proposed rule on incentive-based compensation arrangements to implement Section 956 of the Dodd-Frank Act. The proposed rule would:

- Prohibit "incentive-based payment arrangements that the Agencies determine encourage inappropriate risks by certain financial institutions by providing excessive compensation or that could lead to material financial loss."
- Require "financial institutions to disclose information concerning incentive-based compensation arrangements to the appropriate Federal regulator."

For more information, see the press release on the SEC's Web site.

SEC Updates Financial Reporting Manual

In March 2016, the Division published an update to its *Financial Reporting Manual* that contains revisions made as of March 17, 2016. The revisions include:

- *Paragraph 2410.8* — Updates to guidance on significance testing related to equity method investments.
- *Topic 10* — Amendments to conform to the FAST Act.
- *Topic 11* — Addition of implementation guidance related to the FASB's and IASB's new revenue standard.

For more information, see Deloitte's March 22, 2016, journal entry.

SEC and FDIC Issue Proposed Rule on Covered Broker-Dealer Provisions

In February 2016, the SEC and FDIC issued a proposed rule that establishes certain "provisions applicable to the orderly liquidation of covered brokers and dealers." The proposal is being issued in response to a mandate of the Dodd-Frank Act.

SEC Publishes Examination Priorities for 2016

In January 2016, the SEC's Office of Compliance Inspections and Examinations published its examination priorities for 2016. New priorities include liquidity controls, public pension advisers, product promotion, exchange-traded funds, and variable annuities. Further, the priorities "reflect a continuing focus on protecting investors in ongoing risk areas such as cybersecurity, microcap fraud, fee selection, and reverse churning."

For more information, see the press release on the SEC's Web site.

2015 AICPA Conference on Current SEC and PCAOB Developments

At the 2015 AICPA Conference on Current SEC and PCAOB Developments, numerous speakers and discussion panels shared their insights into current accounting, reporting, and auditing practice issues. Key topics addressed at the event included the following:

- *Disclosure effectiveness* — Speakers focused on improving disclosure requirements, with the goal of enhancing the information provided to investors and promoting efficiency, competition, and capital formation. The SEC reiterated its continued focus on disclosure effectiveness, including its outreach to the investor community and its ongoing collaboration with the FASB.
- *ICFR* — This topic continues to be a key focus for regulators, preparers, and auditors. SEC Chief Accountant James Schnurr stated that "[m]anagement's ability to fulfill its financial reporting responsibilities depends, in large part, on the design and effectiveness of internal control over financial reporting." Several speakers commented that the frequency of ICFR-related findings in PCAOB inspections highlights the need for management, auditors, and audit committees to work together to address potential underlying issues with controls and assessments.

- *IFRSs* — The SEC's consideration of the potential incorporation of IFRSs into the U.S. financial reporting system has long been a topic at the conference, and this year was no exception. At the 2014 conference, Mr. Schnurr introduced a potential fourth alternative regarding the use of IFRSs in the United States that would allow U.S.-based filers to voluntarily provide supplemental IFRS-based information without reconciliation to U.S. GAAP. In his remarks at the 2015 conference, Mr. Schnurr indicated that the OCA is likely to recommend that the SEC consider and commence rulemaking that is consistent with this fourth alternative.
- *Audit committees* — Speakers observed that the roles and responsibilities now frequently imposed on audit committees in addition to their core SEC-required duties may interfere with their primary responsibility of overseeing the company's financial reporting. Mr. Schnurr recapped the SEC staff's efforts over the past year to address "whether investors are interested in hearing from audit committees on *how* (not just *if*) they have fulfilled their responsibilities; and . . . whether the Commission's rules support such reporting." As part of these efforts, the SEC issued a concept release in July 2015 to seek feedback on the proposed changes to the reporting requirements as well as on additional disclosures investors may want.

For more information, see Deloitte's December 15, 2015, *Heads Up*.

SEC Proposes Rule on Use of Derivatives

In December 2015, the SEC issued a proposed rule on use of derivatives by registered investment companies and business development companies. The proposal would "place restrictions on funds, such as mutual funds and exchange-traded funds . . . that would limit their use of derivatives and require funds to put in place risk management measures resulting in better protection for investors."

For more information, see the press release on the SEC's Web site.

SEC Proposes Enhancements to Disclosure Requirements for Alternative Trading Systems

In November 2015, the SEC issued a proposed rule that would amend the requirements for alternative trading systems under the Exchange Act. Specifically, the proposal would require alternative trading systems that "trade stocks listed on a national securities exchange (NMS stocks), including 'dark pools,' to publicly disclose detailed information about the operations and activities of a broker-dealer operator and its affiliates."

For more information, see the press release on the SEC's Web site.

Summary of Accounting Pronouncements Effective in 2016

The table below lists ASUs that became effective for calendar year 2016. (Note that it is assumed that the ASUs were not early adopted before 2016 if early adoption was permitted.)

ASU (Issuance Month)	Affects	Effective Date for Public Business Entities	Effective Date for All Other Entities
ASU 2016-03, *Intangibles — Goodwill and Other (Topic 350), Business Combinations (Topic 805), Consolidation (Topic 810), Derivatives and Hedging (Topic 815): Effective Date and Transition Guidance* — a consensus of the Private Company Council (March 2016)	Private entities.	Not applicable.	Upon issuance.
ASU 2015-16, *Simplifying the Accounting for Measurement-Period Adjustments* (September 2015)	Entities that have reported provisional amounts for items in a business combination for which the accounting is incomplete by the end of the reporting period in which the business combination occurs and during the measurement period have an adjustment to provisional amounts recognized.	Fiscal years (and interim periods therein) beginning after December 15, 2015.	Fiscal years beginning after December 15, 2016, and interim periods within fiscal years beginning after December 15, 2017.
ASU 2015-12, *(Part I) Fully Benefit-Responsive Investment Contracts, (Part II) Plan Investment Disclosures, (Part III) Measurement Date Practical Expedient* — consensuses of the FASB Emerging Issues Task Force (July 2015)	Reporting entities within the scope of ASC 960, ASC 962, or ASC 965. Effective for fiscal years beginning after December 15, 2015.		

(Table continued)

ASU (Issuance Month)	Affects	Effective Date for Public Business Entities	Effective Date for All Other Entities
ASU 2015-10, *Technical Corrections and Improvements* (June 2015)	All entities.	Transition guidance varies on the basis of the amendments in the ASU. The amendments that require transition guidance are effective for all entities for fiscal years and interim periods within those fiscal years beginning after December 15, 2015.	
ASU 2015-09, *Disclosures About Short-Duration Contracts* (May 2015)	All insurance entities that issue short-duration contracts as defined in ASC 944. The amendments do not apply to the holder (i.e., policyholder) of short-duration contracts.	Fiscal years beginning after December 15, 2015, and interim periods within annual periods beginning after December 15, 2016.	Fiscal years beginning after December 15, 2016, and interim periods within annual periods beginning after December 15, 2017.
ASU 2015-07, *Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)* — a consensus of the FASB Emerging Issues Task Force (May 2015)	All entities.	Fiscal years (and interim periods therein) beginning after December 15, 2015.	Fiscal years (and interim periods therein) beginning after December 15, 2016.
ASU 2015-06, *Effects on Historical Earnings per Unit of Master Limited Partnership Dropdown Transactions* — a consensus of the FASB Emerging Issues Task Force (April 2015)	All entities.	Fiscal years (and interim periods therein) beginning after December 15, 2015.	
ASU 2015-05, *Customer's Accounting for Fees Paid in a Cloud Computing Arrangement* (April 2015)	All entities.	Annual periods (and interim periods therein) beginning after December 15, 2015.	Annual periods beginning after December 15, 2015, and interim periods within annual periods beginning after December 15, 2016.
ASU 2015-04, *Practical Expedient for the Measurement Date of an Employer's Defined Benefit Obligation and Plan Assets* (April 2015)	All entities.	Fiscal years (and interim periods therein) beginning after December 15, 2015.	Fiscal years beginning after December 15, 2016, and interim periods within fiscal years beginning after December 15, 2017.

(Table continued)

ASU (Issuance Month)	Affects	Effective Date for Public Business Entities	Effective Date for All Other Entities
ASU 2015-03, *Simplifying the Presentation of Debt Issuance Costs* (April 2015)	All entities.	Fiscal years (and interim periods therein) beginning after December 15, 2015.	Fiscal years beginning after December 15, 2015, and interim periods within fiscal years beginning after December 15, 2016.
ASU 2015-02, *Amendments to the Consolidation Analysis* (February 2015)	Entities that are required to evaluate whether they should consolidate certain legal entities.	Fiscal years (and interim periods therein) beginning after December 15, 2015.	Fiscal years beginning after December 15, 2016, and for interim periods within fiscal years beginning after December 15, 2017.
ASU 2015-01, *Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items* (January 2015)	All entities.	Fiscal years (and interim periods therein) beginning after December 15, 2015.	
ASU 2014-18, *Accounting for Identifiable Intangible Assets in a Business Combination* — a consensus of the Private Company Council (December 2014)	All entities **except** public business entities and not-for-profit entities, as those terms are defined in the ASC master glossary.	Not applicable.	If the first in-scope transaction occurs in the first fiscal year beginning after December 15, 2015, the elective adoption will be effective for that fiscal year's annual financial reporting and all interim and annual periods thereafter. If the first transaction occurs in fiscal years beginning after December 15, 2016, the elective adoption will be effective in the interim period that includes the date of the transaction and subsequent interim and annual periods thereafter.
ASU 2014-16, *Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share Is More Akin to Debt or to Equity* — a consensus of the FASB Emerging Issues Task Force (November 2014)	Entities that are issuers of, or investors in, hybrid financial instruments that are issued in the form of a share.	Fiscal years (and interim periods therein) beginning after December 15, 2015.	Fiscal years beginning after December 15, 2015, and interim periods within fiscal years beginning after December 15, 2016.

(Table continued)

ASU (Issuance Month)	Affects	Effective Date for Public Business Entities	Effective Date for All Other Entities
ASU 2014-13, *Measuring the Financial Assets and the Financial Liabilities of a Consolidated Collateralized Financing Entity* — a consensus of the FASB Emerging Issues Task Force (August 2014)	A reporting entity that is required to consolidate a collateralized financing entity under the variable interest entities subsections of ASC 810-10 and that measures assets and liabilities of the collateralized financing entity by using fair value.	Fiscal years (and interim periods therein) beginning after December 15, 2015.	Fiscal years **ending** after December 15, 2016, and interim periods **beginning** after December 15, 2016.
ASU 2014-12, *Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved After the Requisite Service Period* — a consensus of the FASB Emerging Issues Task Force (June 2014)	Reporting entities that grant their employees share-based payments in which the terms of the award stipulate that a performance target that affects vesting could be achieved after the requisite service period.	Fiscal years (and interim periods therein) beginning after December 15, 2015.	

Appendixes

Appendix A — Glossary of Standards and Other Literature

The following are the titles of standards and other literature mentioned in this publication:

FASB ASUs

ASU 2016-17, *Consolidation (Topic 810): Interests Held Through Related Parties That Are Under Common Control*

ASU 2016-16, *Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory*

ASU 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments* — a consensus of the Emerging Issues Task Force

ASU 2016-13, *Financial Instruments — Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*

ASU 2016-12, *Revenue From Contracts With Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients*

ASU 2016-11, *Revenue Recognition (Topic 605) and Derivatives and Hedging (Topic 815): Rescission of SEC Guidance Because of Accounting Standards Updates 2014-09 and 2014-16 Pursuant to Staff Announcements at the March 3, 2016 EITF Meeting (SEC Update)*

ASU 2016-10, *Revenue From Contracts With Customers (Topic 606): Identifying Performance Obligations and Licensing*

ASU 2016-09, *Compensation — Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting*

ASU 2016-08, *Revenue From Contracts With Customers (Topic 606): Principal Versus Agent Considerations (Reporting Revenue Gross Versus Net)*

ASU 2016-07, *Investments — Equity Method and Joint Ventures (Topic 323): Simplifying the Transition to the Equity Method of Accounting*

ASU 2016-06, *Derivatives and Hedging (Topic 815): Contingent Put and Call Options in Debt Instruments* — a consensus of the Emerging Issues Task Force

ASU 2016-05, *Derivatives and Hedging (Topic 815): Effect of Derivative Contract Novations on Existing Hedge Accounting Relationships* — a consensus of the Emerging Issues Task Force

ASU 2016-04, *Liabilities — Extinguishments of Liabilities (Subtopic 405-20): Recognition of Breakage for Certain Prepaid Stored-Value Products* — a consensus of the Emerging Issues Task Force

ASU 2016-03, *Intangibles — Goodwill and Other (Topic 350), Business Combinations (Topic 805), Consolidation (Topic 810), Derivatives and Hedging (Topic 815): Effective Date and Transition Guidance* — a consensus of the Private Company Council

ASU 2016-02, *Leases (Topic 842)*

ASU 2016-01, *Financial Instruments — Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*

ASU 2015-17, *Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes*

ASU 2015-16, *Business Combinations (Topic 805): Simplifying the Accounting for Measurement-Period Adjustments*

ASU 2015-14, *Revenue From Contracts With Customers (Topic 606): Deferral of the Effective Date*

ASU 2015-12, *Plan Accounting: Defined Benefit Pension Plans (Topic 960), Defined Contribution Pension Plans (Topic 962), Health and Welfare Benefit Plans (Topic 965): (Part I) Fully Benefit-Responsive Investment Contracts, (Part II) Plan Investment Disclosures, (Part III) Measurement Date Practical Expedient* — consensuses of the FASB Emerging Issues Task Force

ASU 2015-10, *Technical Corrections and Improvements*

ASU 2015-09, *Financial Services — Insurance (Topic 944): Disclosures About Short-Duration Contracts*

ASU 2015-07, *Fair Value Measurement (Topic 820): Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)* — a consensus of the FASB Emerging Issues Task Force

ASU 2015-06, *Earnings per Share (Topic 260): Effects on Historical Earnings per Unit of Master Limited Partnership Dropdown Transactions* — a consensus of the FASB Emerging Issues Task Force

ASU 2015-05, *Intangibles — Goodwill and Other — Internal-Use Software (Subtopic 350-40): Customer's Accounting for Fees Paid in a Cloud Computing Arrangement*

ASU 2015-04, *Compensation — Retirement Benefits (Topic 715): Practical Expedient for the Measurement Date of an Employer's Defined Benefit Obligation and Plan Assets*

ASU 2015-03, *Interest — Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs*

ASU 2015-02, *Consolidation (Topic 810): Amendments to the Consolidation Analysis*

ASU 2015-01, *Income Statement — Extraordinary and Unusual Items (Subtopic 225-20): Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items*

ASU 2014-18, *Business Combinations (Topic 805): Accounting for Identifiable Intangible Assets in a Business Combination* — a consensus of the Private Company Council

ASU 2014-16, *Derivatives and Hedging (Topic 815): Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share Is More Akin to Debt or to Equity* — a consensus of the FASB Emerging Issues Task Force

ASU 2014-13, *Consolidation (Topic 810): Measuring the Financial Assets and the Financial Liabilities of a Consolidated Collateralized Financing Entity* — a consensus of the FASB Emerging Issues Task Force

ASU 2014-12, *Compensation — Stock Compensation (Topic 718): Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period* — a consensus of the FASB Emerging Issues Task Force

ASU 2014-09, *Revenue From Contracts With Customers (Topic 606)*

ASU 2014-07, *Consolidation (Topic 810): Applying Variable Interest Entities Guidance to Common Control Leasing Arrangements* — a consensus of the Private Company Council

ASU 2014-03, *Derivatives and Hedging (Topic 815): Accounting for Certain Receive-Variable, Pay-Fixed Interest Rate Swaps — Simplified Hedge Accounting Approach* — a consensus of the Private Company Council

ASU 2014-02, *Intangibles — Goodwill and Other (Topic 350): Accounting for Goodwill* — a consensus of the Private Company Council

ASU 2010-20, *Receivables (Topic 310): Disclosures About the Credit Quality of Financing Receivables and the Allowance for Credit Losses*

FASB ASC Topics and Subtopics

ASC 230, *Statement of Cash Flows*

ASC 235, *Notes to Financial Statements*

ASC 250, *Accounting Changes and Error Corrections*

ASC 250-10, *Accounting Changes and Error Corrections: Overall*

ASC 310, *Receivables*

ASC 310-30, *Receivables: Loans and Debt Securities Acquired With Deteriorated Credit Quality*

ASC 310-940, *Receivables: Financial Services — Brokers and Dealers*

ASC 320, *Investments — Debt and Equity Securities*

ASC 320-940, *Investments — Debt and Equity Securities: Financial Services — Brokers and Dealers*

ASC 321, *Investments — Equity Securities*

ASC 321-10, *Investments — Equity Securities: Overall*

ASC 323, *Investments — Equity Method and Joint Ventures*

ASC 325, *Investments — Other*

ASC 325-40, *Investments — Other: Beneficial Interests in Securitized Financial Assets*

ASC 326, *Financial Instruments — Credit Losses*

ASC 326-30, *Financial Instruments — Credit Losses: Available-for-Sale Debt Securities*

ASC 350, *Intangibles — Goodwill and Other*

ASC 360, *Property, Plant, and Equipment*

ASC 360-20, *Property, Plant, and Equipment: Real Estate Sales*

ASC 405, *Liabilities*

ASC 405-20, *Liabilities: Extinguishments of Liabilities*

ASC 460, *Guarantees*

ASC 470-20, *Debt: Debt With Conversion and Other Options*

ASC 480, *Distinguishing Liabilities From Equity*

ASC 480-10, *Distinguishing Liabilities From Equity: Overall*

ASC 505-50, *Equity: Equity-Based Payments to Non-Employees*

ASC 605, *Revenue Recognition*

ASC 605-20, *Revenue Recognition: Services*

ASC 605-25, *Revenue Recognition: Multiple-Element Arrangements*

ASC 605-45, *Revenue Recognition: Principal Agent Considerations*

ASC 605-50, *Revenue Recognition: Customer Payments and Incentives*

ASC 606, *Revenue From Contracts With Customers*

ASC 606-10, *Revenue From Contracts With Customers: Overall*

ASC 610-20, *Other Income: Gains and Losses From the Derecognition of Nonfinancial Assets*

ASC 715, *Compensation — Retirement Benefits*

ASC 715-20, *Compensation — Retirement Benefits: Defined Benefit Plans — General*

ASC 718, *Compensation — Stock Compensation*

ASC 740, *Income Taxes*

ASC 740-10, *Income Taxes: Overall*

ASC 805, *Business Combinations*

ASC 805-10, *Business Combinations: Overall*

ASC 815, *Derivatives and Hedging*

ASC 815-15, *Derivatives and Hedging: Embedded Derivatives*

ASC 815-20, *Derivatives and Hedging: Hedging — General*

ASC 815-40: *Derivatives and Hedging: Contracts in Entity's Own Equity*

ASC 820, *Fair Value Measurement*

ASC 820-10, *Fair Value Measurement: Overall*

ASC 825, *Financial Instruments*

ASC 825-10, *Financial Instruments: Overall*

ASC 840, *Leases*

ASC 860, *Transfers and Servicing*

ASC 924-405, *Entertainment — Casinos: Liabilities*

ASC 932-10, *Extractive Activities — Oil and Gas: Overall*

ASC 946, *Financial Services — Investment Companies*

ASC 958, *Not-for-Profit Entities*

ASC 960, *Plan Accounting — Defined Benefit Pension Plans*

ASC 962, *Plan Accounting — Defined Contribution Pension Plans*

ASC 965, *Plan Accounting — Health and Welfare Benefit Plans*

ASC 970-605, *Real Estate — General: Revenue Recognition*

FASB Proposed ASUs

Proposed ASU 2016-340, *Receivables — Nonrefundable Fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt Securities*

Proposed ASU 2016-320, *Technical Corrections and Improvements to Update No. 2014-09, Revenue From Contracts With Customers (Topic 606) — Additional Corrections*

Proposed ASU 2016-310, *Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities*

Proposed ASU EITF-16B, *Plan Accounting — Defined Benefit Pension Plans (Topic 960), Defined Contribution Pension Plans (Topic 962), Health and Welfare Benefit Plans (Topic 965): Employee Benefit Plan Master Trust Reporting* — a consensus of the Emerging Issues Task Force

Proposed ASU 2016-270, *Income Taxes (Topic 740): Disclosure Framework — Changes to the Disclosure Requirements for Income Taxes*

Proposed ASU 2016-250, *Other Income — Gains and Losses From the Derecognition of Nonfinancial Assets (Subtopic 610-20): Clarifying the Scope of Asset Derecognition Guidance and Accounting for Partial Sales of Nonfinancial Assets*

Proposed ASU 2016-240, *Technical Corrections and Improvements to Update 2014-09, Revenue From Contracts With Customers (Topic 606)*

Proposed ASU 2016-230, *Intangibles — Goodwill and Other (Topic 350): Simplifying the Accounting for Goodwill Impairment*

Proposed ASU EITF-16A, *Statement of Cash Flows (Topic 320): Restricted Cash*

Proposed ASU 2016-210, *Compensation — Retirement Benefits — Defined Benefit Plans —General (Subtopic 715-20): Changes to the Disclosure Requirements for Defined Benefit Plans*

Proposed ASU 2016-200, *Compensation — Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*

Proposed ASU 2015-350, *Fair Value Measurement (Topic 820): Disclosure Framework — Changes to the Disclosure Requirements for Fair Value Measurement*

Proposed ASU 2015-330, *Business Combinations (Topic 805): Clarifying the Definition of a Business*

Proposed ASU 2015-340, *Government Assistance (Topic 832): Disclosures by Business Entities About Government Assistance*

Proposed ASU 2015-310, *Notes to Financial Statements (Topic 235): Assessing Whether Disclosures Are Material*

Proposed ASU 2015-280, *Investments — Equity Method and Joint Ventures (Topic 323): Simplifying the Equity Method of Accounting*

Other FASB Proposals

Invitation to Comment 2016-290, *Agenda Consultation*

Proposed Concepts Statement 2015-300, *Conceptual Framework for Financial Reporting: Chapter 3: Qualitative Characteristics of Useful Financial Information*

Proposed Concepts Statement 2014-200, *Conceptual Framework for Financial Reporting: Chapter 8: Notes to Financial Statements*

Invitation to Comment 2012-220, *Disclosure Framework*

FASB Concepts Statement

CON 8, *Conceptual Framework for Financial Reporting*

EITF Issues

15-F, "Statement of Cash Flows: Classification of Certain Cash Receipts and Cash Payments"

16-A, " 'Restricted Cash' (previously included in EITF Issue No. 15-F, 'Statement of Cash Flows: Classification of Certain Cash Receipts and Cash Payments')"

16-B, "Employee Benefit Plan Master Trust Reporting"

Private Company Council Literature

PCC Issue No. 15-02, "Applying Variable Interest Entity Guidance to Entities Under Common Control"

SEC Division of Corporation Finance *Financial Reporting Manual*

Topic 2, "Other Financial Statements Required"; Section 2400, "Equity Method Investments, Including Fair Value Option"

Topic 10, "Emerging Growth Companies"

Topic 11, "Reporting Issued Related to Adoption of New Revenue Recognition Standard"

Topic 13, "Effects of Subsequent Events on Financial Statements Required in Filings"

SEC Regulation AB (Asset-Backed Securities)

Item 1101(c), "Definitions; Asset-Backed Security"

SEC Regulation S-X

Rule 4-08(h), "General Notes to Financial Statements: Income Tax Expense"

SEC Regulation S-K

Item 402(c), "Executive Compensation; Summary Compensation Table"

Item 507, "Selling Security Holders"

SEC Final Rules

34-78961, *Standards for Covered Clearing Agencies*

34-78716, *Access to Data Obtained by Security-Based Swap Data Repositories*

IA-4509, *Form ADV and Investment Advisers Act Rules*

34-78321, *Regulation SBSR — Reporting and Dissemination of Security-Based Swap Information*

IA-4439, *Adviser Business Continuity and Transition Plans*

34-78011, *Trade Acknowledgment and Verification of Security-Based Swap Transactions*

34-77617, *Business Conduct Standards for Security-Based Swap Dealers and Major Security-Based Swap Participants*

SIPA-175, *Securities Investor Protection Corporation*

34-77104, *Security-Based Swap Transactions Connected With a Non-U.S. Person's Dealing Activity That Are Arranged, Negotiated, or Executed by Personnel Located in a U.S. Branch or Office or in a U.S. Branch or Office of an Agent; Security-Based Swap Dealer* De Minimis *Exception*

SEC Interim Final Rules

34-77969, Request for Comment, *Form 10-K Summary*

33-10003, Request for Comment, *Simplification of Disclosure Requirements for Emerging Growth Companies and Forward Incorporation by Reference on Form S-1 for Smaller Reporting Companies*

SEC Proposed Rules and Concept Releases

34-78963, *Definition of "Covered Clearing Agency"*

34-78962, *Amendment to Securities Transaction Settlement Cycle*

34-78309, *Disclosure of Order Handling Information*

33-10110, *Disclosure Update and Simplification*

33-10107, *Amendments to Smaller Reporting Company Definition*

33-10064, *Business and Financial Disclosure Required by Regulation S-K*

34-77776, *Incentive-Based Compensation Arrangements*

34-77157, *Covered Broker-Dealer Provisions Under Title II of the Dodd-Frank Wall Street Reform and Consumer Protection Act*

34-76474, *Regulation of NMS Stock Alternative Trading Systems*

33-9862, *Possible Revisions to Audit Committee Disclosures*

Other SEC Proposal

33-10198, *Request for Comment on Subpart 400 of Regulation S-K Disclosure Requirements Relating to Management, Certain Security Holders and Corporate Governance Matters*

SEC Staff Accounting Bulletin

SAB Topic 13, "Revenue Recognition"

SEC Office of Compliance Inspections and Examinations

Examination Priorities for 2016

SEC C&DI Topics

Exchange Act Sections 13(d) and 13(g) and Regulation 13D-G Beneficial Ownership Reporting

Non-GAAP Financial Measures

Regulation AB and Related Rules

Regulation S-K

Securities Act Forms

Securities Act Rules

Securities Act Sections

Securities Act of 1933 Rule

Rule 501(a), "Definitions and Terms Used in Regulation D; Accredited Investor"

Securities Exchange Act of 1934 Rules

Rule 10b-10 "Manipulative and Deceptive Devices and Contrivances; Confirmation of Transactions"

Rule 12g "Extensions and Temporary Exemptions":

- Rule 12g-1, "Definitions; Exemption From Section 12(g)"
- Rule 12g-2, "Securities Deemed to Be Registered Pursuant to Section 12(g)(1) Upon Termination of Exemption Pursuant to Section 12(g)(2) (A) or (B)"
- Rule 12g-3, "Registration of Securities of Successor Issuers Under Section 12(b) or 12(g)"
- Rule 12g-4, "Certifications of Termination of Registration Under Section 12(g)"

Rule 12h-3, "Suspension of Duty to File Reports Under Section 15(d)"

Rule 13n-4, "Regulation SBSR; Duties and Core Principles of Security-Based Swap Data Repository"

Rule 15c3-1, "Rules Relating to Over-the-Counter Markets; Net Capital Requirements for Brokers or Dealers"

Rule 17a-5(e)(4), "Reports to Be Made by Certain Brokers and Dealers: Nature and Form of Reports"

International Standards

IFRS 16, *Leases*

IFRS 15, *Revenue From Contracts With Customers*

IAS 17, *Leases*

IAS 12, *Income Taxes*

Appendix B — Abbreviations

Abbreviation	Description
AFS	available for sale
AICPA	American Institute of Certified Public Accountants
AOCI	accumulated other comprehensive income
APIC	additional paid-in capital
ASC	FASB Accounting Standards Codification
ASU	FASB Accounting Standards Update
ATM	automated teller machine
AUP	agreed-upon procedures
BOLI	bank-owned life insurance
C&DI	SEC compliance and disclosure interpretation
CACM	consistently applied compensation measure
CECL	current expected credit loss
COLI	corporate-owned life insurance
DTA	deferred tax asset
DTL	deferred tax liability
EGC	emerging growth company
EITF	Emerging Issues Task Force
EPS	earnings per share
FASB	Financial Accounting Standards Board
FDIC	Federal Deposit Insurance Corporation
FHFA	Federal Housing Finance Agency
FINRA	Financial Industry Regulatory Authority

Abbreviation	Description
GAAP	generally accepted accounting principles
GP	general partner
HTM	held to maturity
IAS	International Accounting Standard
IASB	International Accounting Standards Board
ICFR	internal control over financial reporting
IFRS	International Financial Reporting Standard
IP	intellectual property
IPO	initial public offering
LGD	loss given default
LP	limited partner
NCUA	National Credit Union Administration
NMS	National Market System
NOL	net operating loss
OCA	SEC's Office of the Chief Accountant
OCC	Office of the Comptroller of the Currency (U.S. Department of the Treasury)
OCI	other comprehensive income
PCAOB	Public Company Accounting Oversight Board
PCC	Private Company Council
PCD asset	purchased financial assets with credit deterioration
PD	probability of default

Abbreviation	Description
ROU	right of use
SAB	SEC Staff Accounting Bulletin
SAC	subjective acceleration clause
SBS	security-based swap
SEC	Securities and Exchange Commission
SIFMA	Securities Industry and Financial Markets Association
SIPC	Securities Investor Protection Corporation
TRG	transition resource group
VIE	variable interest entity

The following is a list of short references for the Acts mentioned in this publication:

Abbreviation	Act
Dodd-Frank Act	Dodd-Frank Wall Street Reform and Consumer Protection Act
Exchange Act	Securities Exchange Act of 1934
FAST Act	Fixing America's Surface Transportation Act
Hart-Scott-Rodino Act	Hart-Scott-Rodino Antitrust Improvements Act
Investment Advisers Act	Investment Advisers Act of 1940
JOBS Act	Jumpstart Our Business Startups Act
Securities Act	Securities Act of 1933

Appendix C — Other Resources

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