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Quarterly Financial Reporting Update: March 2019

Tuesday, March 26, 2019
1:00 – 2:00 pm CT

We will be starting soon

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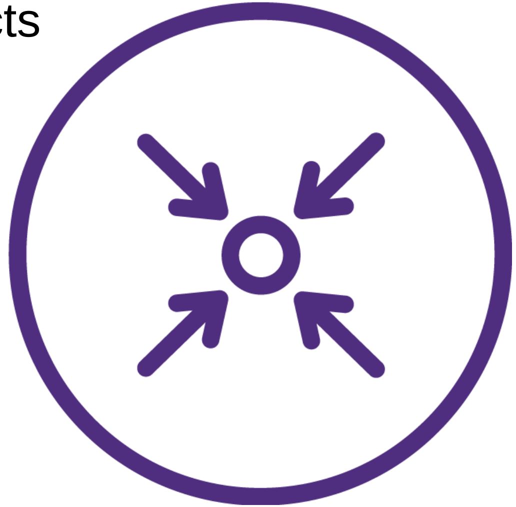
Learning objectives

- Recognize the potential impact of recently issued standards on your company
- Describe the current status of standard-setting projects
- Identify recent news and events that may affect financial reporting



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Agenda

- Leases
- Revenue recognition
- CECL
- Current reporting topics
- FASB project update
- Audit topics

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Leases

ASU 2019-01 Codification improvements

- Lessors that are not manufacturers or dealers may use cost to determine the fair value of the underlying asset
- Depository or lending institution lessors may present cash receipts for principal payments on sales-type or finance leases as investing activities instead of operating in the statement of cash flows
- All entities are exempt from making certain transition disclosures in ASC 250 *Accounting Changes and Error Corrections,* in interim as well as annual periods

ASC 250 requires disclosure of impact on income from continuing operations, net income, other affected financial statement line item, and per share amounts

Disclosures were not required in **annual periods**, now also not required in **interim periods**

Incremental borrowing rate

Incremental borrowing rate must reflect:

- Amount and timing of lease payments
- Fully collateralized
- Lease term
- Economic environment

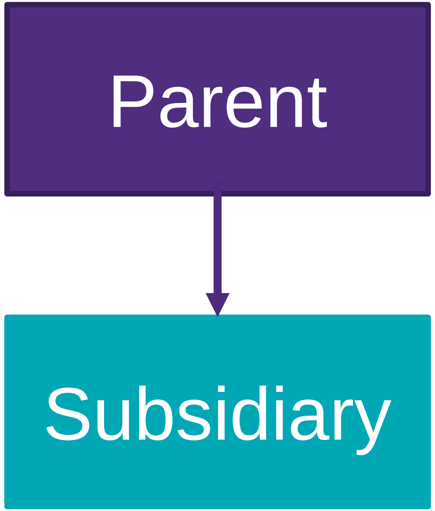
Estimate may involve adjusting a reference rate available to the entity to satisfy the incremental borrowing rate criteria.

Reference rates could include:

- Rate on lessee's existing debt facility
- Borrowing rate of entities similar to the lessee
- Rate quoted by a lender or lenders

Incremental borrowing rate – Subsidiary use of parent's rate

May be appropriate if the pricing of the lease is **more significantly influenced** by the parent's credit standing than the subsidiary's credit standing



For more discussion of the incremental borrowing rate, see Grant Thornton's *Snapshot 2019-01 Practice issue: Lessee accounting under ASC 842*

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Determining the lease term

The lease term includes the noncancellable term, and reflects the impact of options to renew or terminate that the lessee is reasonably certain to exercise or not exercise, plus any lessor options

In determining if a lessee is reasonably certain to exercise a renewal option, factors to consider include:

- Economic incentive to extend, including significant leasehold improvements or a residual value guarantee
- How central the underlying asset is to the entity's operations
- the availability of similar assets in the marketplace
- The entity's plans and the economic environment

General leasing disclosures

Disclosure objective: To enable users of financial statements to assess the amount, timing, and uncertainty of cash flows arising from leases

All entities must disclose information about:

- The entity's leases
- The significant judgments made in accounting for leases
- The amounts recognized in the financial statements related to leases

Lessee disclosure reminders

For all leases

- Information about leases (including subleases)
- Leases not yet commenced
- Significant judgements and assumptions
- Related party leasing activities
- Accounting policy elections

Separately for finance and operating leases

- Lease cost (operating, finance, short term, variable)
- Cash and noncash information about increases and decreases in lease liabilities
- Weighted-average remaining lease term and discount rate
- Maturity analysis of lease liabilities, including a reconciliation of undiscounted cash flows to the liabilities on the balance sheet

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Lessor disclosure reminders

Lessor are required to disclose

- Information about leases
- Significant assumptions and judgements
- Practical expedient to not separate components
- Lease income
- Related parties
- Management of risk related to residual assets
- Disclosure specific to sales-type and direct financing leases
- Disclosures specific to operating leases

Revenue recognition

Revenue recognition

ASC 606 implementation lessons learned

- Policies, processes, and controls across the organization will require updates
- Cross functional involvement is key
- Early discussions with, stakeholders, auditors and those charged with governance
- New disclosures require significant planning and effort

Private company revenue implementation

Plan

- Understand impact across organization
- Evaluate revenue streams to identify initial potential impact
- Review organizational processes
- Identify income tax changes and reporting requirements
- Finalize milestone-level implementation plan

Assess

- Complete detailed assessment of all revenue streams
- Draft and review changes with internal and external auditors
- Identify and draft changes to internal controls
- Tax changes prepared and communications with relevant authorities identified

Design

- Design changes to processes and systems
- Obtain agreement with auditors on technical accounting impact
- Identify required tax reporting changes
- Plan communication of changes and impact on the organization
- Reset forecasts, budgeting, bank covenants, expectations with users

Execute

- Implement, manage, and monitor accounting, process and system changes
- Provide proper tax authority communications
- Roll out new customer contract terms and conditions
- Manage communications of change drivers and related impacts

CECL

FASB Q&A on credit loss reserves

The **weighted average remaining maturity (WARM) method** is a loss rate method that may be an acceptable method for calculating expected credit losses for certain pools of financial assets

1. Determine annual amortized cost of the pool of financial assets
2. Calculate and apply average annual charge-off rate
3. Adjust for qualitative factors

FASB Q&A discusses considerations an entity can make in determining if use of the WARM method may be appropriate, as well as how the WARM method could be applied to an example pool of financial assets.

Factors when considering use of the WARM method

	Use of the WARM method may be:	
Factors	**More appropriate**	**Less appropriate**
Asset pool	Less complex, larger in size, homogeneous make up	More complex, smaller in size, more varied make up
Historical loss data	Lots of data on historical losses, losses occur in predictive patterns	Limited data on historical losses, losses are sporadic with no predictive patterns
Economic environment	Stable economic environment	Changes in the economic environment

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Current reporting topics

SEC final rule: FAST Act Modernization and Simplification of Regulation S-K

Intended to improve readability and navigability of disclosures and discourage duplication and disclosure of immaterial information

Generally permits exclusion of discussion of the earliest of the three years in MD&A, if such discussion was included in a prior SEC filing	Allows omission of certain confidential information from exhibits without a request for confidential treatment	Other amendments include a requirement to tag cover page data in Inline XBRL and limit property disclosures to those material to the registrant

For more information, refer to forthcoming “New Developments Summary” publication

Form 10-Q: Statement of changes in stockholders' equity

Required beginning Q1 2019 for calendar year-end registrants

- Separate statement or in the notes to the financial statements
- Current and comparative prior year quarter-to-date and year-to-date periods in the form of a reconciliation
- Dividends per share and in aggregate for each class of shares

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Tax reform practice issue

December 2018

OMB and Treasury Department concluded that refundable alternative minimum tax (AMT) credits are not subject to sequestration

January 2019

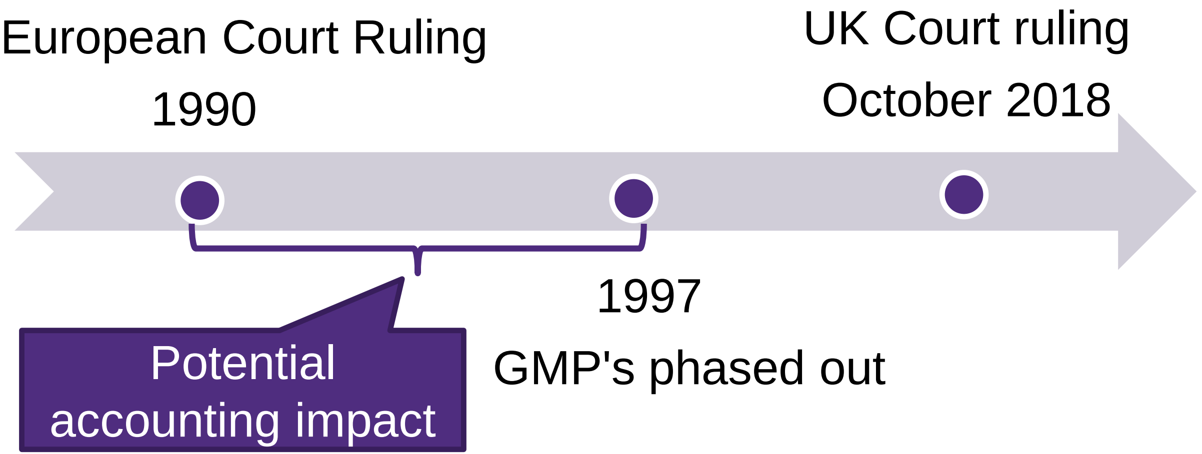
IRS updated its publication, "Effect of Sequestration on the Alternative Minimum Tax Credit for Corporations" to formalize this decision

- Reevaluate realizablitiy of deferred tax assets for refundable AMT credits in financial statements not yet issued
- Determine if sufficient positive evidence was available in December 2018 to support the removal of a valuation allowance

UK benefit plan practice issue

A United Kingdom High Court ruled that a 1990 European Court requirement for pension plans to provide equal benefits to men and women applies to UK Guaranteed Minimum Pension Schemes, or GMP's

Account for resulting changes to benefit obligations as either a change in actuarial assumptions or a plan amendment



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FASB project update

Recently issued accounting standards

ASU 2019-02, *Improvements to Accounting for Costs of Films and License Agreements for Program Materials*

- Applies to broadcasters and entities that produce and distribute episodic television
- Aligns accounting for production costs of an episodic television series with accounting for similar costs for films

ASU 2019-03, *Updating the Definition of Collections*

- Applies to entities that maintain a collection as defined in ASC 958
- Allows an entity to adopt an accounting policy to use proceeds from the sale of a collection item for the direct care of the collection

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Assumed liability in a revenue contract

Proposed ASU

- For entities entering business combinations after adoption of ASC 606
- Acquirer would recognize an assumed liability from a contract with a customer if:
  - It meets the definition of an unsatisfied performance obligation
  - Consideration has been received or is due from the customer

Invitation to comment

- Payment terms and their effect on subsequent revenue recognized
- Costs to fulfill a performance obligation in measuring contract liability
- Examples demonstrating potential effect of including explicit guidance on these matters

All comments are due April 30, 2019

Assumed liability in a revenue contract - example

Effect of payment terms on subsequent revenue recognition

- Assume the contract begins 1/1/X9 and the business combination is 1/2/X9
- Fair value of unsatisfied performance obligation: $900
- Contract price: $1,000

Scenario	Contract liab. pre 805	Contract liab. post 805	Revenue – no GAAP guidance	Revenue – GAAP guidance
Upfront payment	$1,000	$900	$900	$900
Over time payment	$0	$0	$1,000	$900*

* Entity recognizes a $100 identifiable asset at the acquisition date for the difference between fair value of the contract and the consideration to be received. This asset unwinds as payments are received.

Share based payments to customers

Proposed ASU

ASU 2018-07 *Improvements to Nonemployee Share-Based Payment Accounting* eliminated guidance for accounting for share-based consideration payable to a customer

Under the proposed standard, share-based consideration payable to a customer:

- Measured and classified under ASC 718 at grant date fair value
- Reflected as a reduction in the transaction price under ASC 606
- Subsequent changes in measurement of the share-based awards are not accounted for as changes in the transaction price, reflected elsewhere in the income statement

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Audit topics

PCAOB – Reporting Critical Audit Matters

- Effective for large accelerated filers with a June 30, 2019 year-end and for all other filers with year-ends after December 15, 2020
- Certain exclusions apply
- Early dialogue among the auditor, audit committee, and management is encouraged
- Resources available through the Center for Audit Quality
- PCAOB guidance issued in mid-March 2019

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Center for Audit Quality Audit Quality Disclosure Framework

Key Principles

- Voluntary and Illustrative
- Flexible
- Provides for Firm-Level Disclosures

Elements of Audit Quality

- Leadership, Culture, and Firm Governance
- Ethics and Independence
- Acceptance and Continuance
- Engagement Team Management
- Audit Engagement Performance
- Monitoring

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Any final questions?

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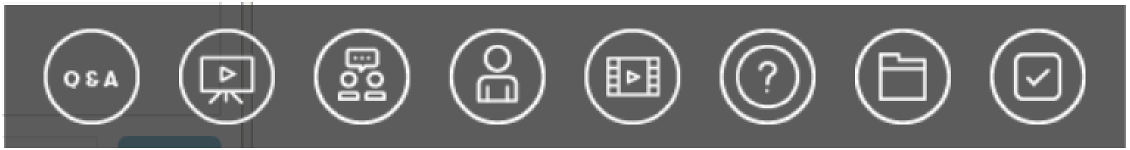

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