ACCOUNTING

A guide to accounting for investments, loans and other receivables

Our publication, A guide to accounting for investments, loans and other receivables under the new guidance affecting the accounting for financial assets, provides a high-level overview of the accounting for investment securities, loans and other receivables and includes the following chapters:

- Chapter 1: Overview
- Chapter 2: Accounting for equity securities
- Chapter 3: Accounting for debt securities
- Chapter 4: Recognition of credit losses on AFS debt securities
- Chapter 5: Accounting for loans and other receivables
- Chapter 6: Recognition and measurement of credit losses on financial assets measured at amortized cost and off-balance-sheet credit exposures
- Chapter 7: Fair value option
- Chapter 8: Presentation and disclosure considerations

Chapter 1 provides an overview of the accounting standards updates (ASUs) affecting the accounting for financial assets issued by the Financial Accounting Standards Board (FASB) in recent years, including (but not limited to) ASU 2016-01, Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities, and ASU 2016-13, Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. Chapter 1 also provides a comparison of preexisting and amended U.S. generally accepted accounting principles to International Financial Reporting Standards for certain types of financial instruments. Each of the remaining chapters begins with a more in-depth summary of the key changes made by the FASB in recent years and then goes on to explain the FASB’s guidance on a particular topic as amended for all recent changes. In addition, numerous examples are provided throughout the guide.

FASB proposes deferred effective dates for leases, CECL and hedging

The Financial Accounting Standards Board (FASB) recently issued a proposed Accounting Standards Update (ASU), Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842): Effective Dates. If finalized, this proposal would defer the effective dates for certain guidance in the FASB Accounting Standards Codification (ASC) for certain entities as follows:
<table>
<thead>
<tr>
<th>Guidance affected</th>
<th>Type of entity</th>
<th>Proposed effective date change</th>
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<tbody>
<tr>
<td>ASC 326, <em>Financial Instruments</em>—<em>Credit Losses</em></td>
<td>SEC filers (as defined in the ASC) other than smaller reporting companies (as defined by the SEC)</td>
<td><strong>No change</strong>: Effective date for an SEC filer that is not a smaller reporting company with a calendar year end continues to be its quarter beginning January 1, 2020.</td>
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<td></td>
<td>Smaller reporting companies</td>
<td><strong>Three-year deferral</strong>: Effective date for a smaller reporting company with a calendar year end will change from its quarter beginning January 1, 2020 to its quarter beginning January 1, 2023.</td>
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<td></td>
<td>All other entities</td>
<td><strong>One- or two-year deferral</strong>: Effective date for an entity other than an SEC filer with a calendar year end will change from its year (and interim period, if applicable) beginning January 1, 2021 or 2022 (as otherwise required) to its year (and interim period, if applicable) beginning January 1, 2023.</td>
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<td>ASC 842, <em>Leases</em></td>
<td>Public business entities (PBEs) (as defined in the ASC); not-for-profit organizations that have issued, or are conduit bond obligors for, securities that are traded, listed, or quoted on an exchange or an over-the-counter market; and employee benefit plans that file financial statements with the SEC</td>
<td><strong>No change</strong>: Effective date for a PBE with a calendar year end continues to be its quarter beginning January 1, 2019.</td>
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<td></td>
<td>All other entities</td>
<td><strong>One-year deferral</strong>: Effective date for all other entities with a calendar year end will change from the year ending December 31, 2020 to the year ending...</td>
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<td>Guidance affected</td>
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<td>Amendments to ASC 815, Derivatives and Hedging</td>
<td>PBEs</td>
<td>No change: Effective date for a PBE with a calendar year end continues to be its quarter beginning January 1, 2019.</td>
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<td></td>
<td>All other entities</td>
<td>One-year deferral: Effective date for an entity other than a PBE with a calendar year end will change from its year ending December 31, 2020 to its year ending December 31, 2021 and interim periods beginning January 1, 2022.</td>
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The Board also will address the effective dates for ASU 2018-12, Financial Services—Insurance (Topic 944): Targeted Improvements to the Accounting for Long-Duration Contracts, as part of a separate project.

The proposed ASU is available for comment until September 16, 2019 and includes information regarding the FASB’s philosophy to simplify how effective dates are staggered between larger public companies and all other entities.

**Proposal: Convertible instruments and contracts in an entity’s own equity**

The Financial Accounting Standards Board recently issued a proposed Accounting Standards Update (ASU) to address the complexity of its guidance for convertible instruments and the derivatives scope exception for contracts in a company’s own equity. If finalized, the proposed ASU would:

- Reduce the number of accounting models for convertible debt instruments and convertible preferred stock. Specifically, the accounting models in ASC 470-20 that require substantial premiums, beneficial conversion features or cash conversion features associated with convertible instruments to be recognized as a separate component of equity would be removed. Only embedded conversion features that are not clearly and closely related to the host contract, meet the definition of a derivative and do not qualify for a scope exception from derivative accounting would continue to be separately recognized (as a derivative).

- Revise the guidance for the derivatives scope exception for conversion features and contracts in an entity’s own equity (e.g., warrants) to reduce form-over-substance-based accounting conclusions driven by remote contingent events. If the likelihood of occurrence is remote, potential adjustments to the settlement terms and contingent events that could require net cash settlement would no longer be considered in the accounting evaluation.

- Amend the related disclosure and earnings-per-share guidance.
The proposed ASU, *Debt – Debt with Conversion and Other Options (Subtopic 470-20) and Derivatives and Hedging – Contracts in Entity’s Own Equity (Subtopic 815-40): Accounting for Convertible Instruments and Contracts in an Entity’s Own Equity*, is available for comment until October 14, 2019.

The interaction between ASC 321, ASC 323 and ASC 815

Topic 321, “Investments—Equity Securities,” of the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) provides the ability to measure certain equity securities without a readily determinable fair value at cost, minus impairment, if any. ASC 321-10-35-2, as amended, states that if an entity identifies observable price changes in orderly transactions for the identical or a similar investment of the same issuer, it should measure the equity security at fair value as of the date that the observable transaction occurred. Diverse views have emerged about the application of this measurement alternative and the equity method of accounting in accordance with ASC 323, “Investments—Equity Method and Joint Ventures.”

The FASB recently issued a proposed Accounting Standards Update (ASU) to clarify that the observable price changes in orderly transactions that should be considered when applying the measurement alternative in accordance with ASC 321 include transactions that require it to either apply or discontinue the equity method of accounting under ASC 323. For example, as it relates to investments for which the measurement alternative is elected, if an observable price change in an orderly transaction for the identical investment or similar security of the same issuer results in a change in ownership that causes the investor to either newly apply or discontinue the equity method, the carrying amount of the security accounted for under the measurement alternative would be adjusted to its fair value immediately before applying or upon discontinuing the equity method.

The proposed ASU also addresses questions about how to apply the guidance in Topic 815, “Derivatives and Hedging,” for certain forward contracts and purchased options to purchase securities that, upon settlement or exercise, would be accounted for under the equity method of accounting. If finalized, the proposed ASU would clarify that, for the purpose of applying ASC 815-10-15-141(a), an entity should not consider whether, upon the settlement of the forward contract or exercise of the purchased option, the underlying securities would be accounted for under the equity method in ASC 323. An entity also would evaluate the remaining characteristics in ASC 815-10-15-141 to determine the accounting for those forward contracts and purchased options.

The proposed ASU is available for comment until August 29, 2019.

SEC

Proposed modernization of Regulation S-K Items 101, 103 and 105

The SEC recently issued a proposed rule, *Modernization of Regulation S-K Items 101, 103, and 105*, which, if finalized, would include the following revisions, among others:

- Item 101(a), *General development of business*, as revised, would:
  - Be largely principles-based by providing a non-exclusive list of the types of information that a registrant may need to disclose, and by requiring disclosure of a topic only to the extent such information is material to an understanding of the general development of a registrant’s business
  - Include as a listed disclosure topic, to the extent material to an understanding of the registrant’s business, transactions and events that affect or may affect the company’s operations
  - Eliminate a prescribed timeframe for this disclosure
  - Permit a registrant, in filings made after its initial filing, to provide only an update of the general development of the business that focuses on material developments in the reporting period, and
with an active hyperlink to the registrant’s most recent filing that, together with the update, would contain the full discussion of the general development of the registrant’s business

- Item 101(c), *Narrative description of business*, as revised, would:
  - Clarify and expand its principles-based approach, by including disclosure topics drawn from a subset of the topics currently in Item 101(c)
  - Include, as a disclosure topic, human capital resources

- Item 103, *Legal proceedings*, as revised, would expressly state that the required information about material legal proceedings may be provided by including hyperlinks or cross-references to legal proceedings disclosure located elsewhere in the document

- Item 105, *Risk factors*, as revised, would:
  - Require summary risk factor disclosure if the risk factor section exceeds 15 pages
  - Change the disclosure standard from the “most significant” factors to the “material” factors required to be disclosed
  - Require risk factors to be organized under relevant headings

**FASB Codification update: SEC disclosure update and simplification**

In 2018 the SEC issued Release No. 33-10532, *Disclosure Update and Simplification*, which amended certain disclosure requirements that had become redundant, outdated or superseded. In this Release, the SEC also referred certain of its disclosure requirements that overlap with, but require incremental information to, generally accepted accounting principles to the Financial Accounting Standards Board (FASB) for potential incorporation into its Accounting Standards Codification. After considering these referred disclosures, the FASB recently issued Accounting Standards Update (ASU) 2019-07, *Codification Updates to SEC Sections - Amendments to SEC Paragraphs Pursuant to SEC Final Rule Releases No. 33-10532, Disclosure Update and Simplification, and Nos. 33-10231 and 33-10442, Investment Company Reporting Modernization, and Miscellaneous Updates*.

In addition to amendments pursuant to Release No. 33-10532, ASU 2019-07 also amends various Codification SEC paragraphs pursuant to Releases Nos. 33-10231 and 33-10442, *Investment Company Reporting Modernization*. Other miscellaneous updates to agree the Codification to the electronic Code of Federal Regulations also were made.

**INTERNATIONAL**

**Proposed amendments to disclosure of accounting policies**

International Accounting Standard (IAS) 1, *Presentation of Financial Statements*, requires companies to disclose their “significant” accounting policies. To clarify the threshold for disclosure, the International Accounting Standards Board recently proposed replacing the reference to “significant” with a requirement to disclose “material” accounting policies. The proposal states that information about an accounting policy is material if, when considered together with other information included in a company’s financial statements, it can influence financial statement users’ decisions about the company.

The Board also proposes (a) additional guidance to IAS 1 to help companies understand what makes an accounting policy material and (b) updates to International Financial Reporting Standard Practice Statement 2, *Making Materiality Judgements*, which add further explanations and examples to help companies apply the concept of materiality in making decisions about accounting policy disclosures.
