EEI & AGA Executive Accounting News Flash

September 2018

Dear Colleagues:

The 2019 effective date of the leases standard for public companies is almost here. Companies are focused on understanding the implications of the FASB's recently issued accounting technical corrections and amendments. Soon, they will need to shift their focus to aspects of adoption beyond the technical accounting, including internal controls over financial reporting and disclosures.

Meanwhile, the FASB's work on other standard-setting projects to simplify and clarify current accounting guidance continues.

In this quarter's edition we summarize the impact of these items and more. For more detail on any of the information provided herein, please click the related links contained within or reach out to:

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Contents

Current Quarter Financial Reporting Matters

Regulatory headlines

SEC approves requirements to use Inline XBRL

The SEC recently approved a final rule requiring public companies to embed XBRL into their quarterly and annual HTML financial statements instead of tagging the data in a separate file.

The compliance dates will be phased in over a three-year transition period. The table shows the compliance dates for fiscal periods ending on or after the effective date.

Type of public company	Compliance dates
Large accelerated filers using US GAAP	June 15, 2019
Accelerated filers using US GAAP	June 15, 2020
All other filers	June 15, 2021

Public companies are required to comply in their first Form 10-Q filed for a fiscal period on or after the compliance date.

SEC adopts amendments to simplify and update disclosure requirements

The SEC recently adopted amendments to certain disclosure requirements that have become duplicative, overlapping, or outdated in light of other Commission disclosure requirements, U.S. GAAP, or changes in environment. These amendments would eliminate certain:

-redundant and duplicative requirements, which require substantially similar disclosures as GAAP or other Commission disclosure requirements

-overlapping requirements, which are related to, but not the same as GAAP or to the Commission disclosure requirements

-outdated requirements, which have become obsolete as a result of the passage of time or changed in the regulatory, business, or technological environment

-superseded requirements, which are inconsistent with recent legislation, more recently updated Commission disclosure requirement, or more recent updated GAAP

Resources: SEC's Disclosure Update and Simplification Final Rule.

SEC proposes amendments to disclosures in certain registered debt offerings

As you may recall, in the fourth quarter of 2017 the SEC issued guidance which ultimately reduced the burden on financial statement preparers (i.e. it eliminated the need for certain periods to be discussed in the MD&A). The SEC has continued with its efforts to reduce disclosures that they believe are not meaningful to investors. As such, in July the SEC proposed amendments to financial disclosures for guarantors and issuers of guaranteed securities and affiliates whose securities collateralize a registrant's securities. The proposal would amend Rules 3-10 and 3-16 of Regulation S-X.

The proposed amendments to Rule 3-10 would:

— allow all consolidated subsidiaries, rather than just those that are wholly owned, to provide disclosures other than those normally required under Rule 3-10;

— replace condensed, consolidating financial information with disclosures about the guarantees, issuers and guarantors;

— allow the parent company to include the required disclosures outside its audited annual and unaudited interim consolidated financial statements in the registration statement covering the offer and sale of securities and related prospectus, and certain Exchange Act reports filed later;

— require the parent company to include disclosures in the notes to its consolidated financial statements for annual and quarterly reports beginning with the annual report for the fiscal year in which it completes its first bona fide sale of the securities; and

— specify that an issuer and guarantors must provide disclosures as long as they have an Exchange Act reporting obligation instead of as long as the guaranteed securities are outstanding.

The proposed amendments to Rule 3-16 would:

— replace the requirement to provide separate financial statements for each affiliate whose securities are pledged as collateral with a requirement to provide disclosures about the affiliates and the collateral arrangement;

— permit a parent company to include the required disclosures outside its audited annual and unaudited interim consolidated financial statements in the registration statement covering the offer and sale of the securities and the related prospectuses, and certain Exchange Act reports filed later; and

Not all Companies in our industry are impacted by this but there are some that will be impacted. Based on outreach to member Companies of EEI and AGA that would be impacted, all believed that this proposal would be helpful. It was decided that the industry will submit a comment letter to the SEC supporting the proposed guidance. Comments are due 60 days after the proposed amendments are published in the Federal Register.

Resources: KPMG's Defining Issues, SEC proposes changes to disclosures in certain registered debt offerings; Proposed SEC Rule

New Standards and Guidance

Leases standard – time is running out

In July, the FASB issued two ASUs updating ASC 842 with Codification technical corrections and targeted improvements. In August, the Board issued an exposure draft on narrow-scope improvements for lessors. While companies will need to take time to understand the new and proposed guidance, they cannot delay their implementation efforts.

Codification improvements

The FASB recently issued its final technical corrections to the leases standard. The amendments clarify certain aspects of ASC 842 but do not make any substantive changes to its core provisions or principles.

Resources: KPMG's Handbook, Leases; KPMG's web article; KPMG's Defining Issues, FASB proposes clarifications and technical corrections to the new leases standard; ASU 2018-10

Targeted improvements

The targeted improvements amendments create an additional transition method, and a lessor practical expedient to not separate lease and non-lease components if specific criteria are met.

Optional transition relief

The new transition method allows companies to use the effective date of the leases standard as the date of initial application on transition.

Companies that elect this transition option will:

- not adjust their comparative period financial information for the effects of ASC 842;
- not make the new required lease disclosures for periods before the effective date; and
- carry forward their ASC 840 disclosures for comparative periods.

Lessor separation of lease and non-lease components

The practical expedient permits lessors to make an accounting policy election by class of underlying asset to not separate lease and non-lease components if two specific criteria are met. Those criteria are:

- the timing and pattern of transfer to the lessee of the lease component and the non-lease component(s) associated with that lease component are the same.
- the lease component, if accounted for separately, would be classified as an operating lease.

If the practical expedient has been elected and a contract includes multiple non- lease components one or more that meet(s) the timing and pattern of transfer criterion and one or more that does(do) not – the lessor combines the non-lease component(s) that meet the first criterion with the lease component and separates non-lease components that do not.

If the non-lease component(s) is(are) the predominant component(s) of the combined component – i.e. because the lessee would reasonably be expected to ascribe more value to the non-lease component(s) – the lessor should account for the combined component under ASC 606, as a single ASC 606 performance obligation, rather than under the leases guidance in ASC 842.

In those cases, the lessor:

- uses the same measure of progress for the combined ASC 606 component as it used when determining eligibility for combination of the lease and non- lease component(s) (generally time-elapsed); and
- accounts for all variable payments related to any good or service, including the lease, that is part of the combined ASC 606 performance obligation under the guidance on variable consideration in ASC 606.

All other combined components are accounted for under ASC 842 as a single lease component. This includes situations in which the lease component and non-lease component(s) are equally significant to the contract. If the combined component is accounted for under ASC 842 as a single lease component, the lease is classified as an operating lease by default; no lease classification test is performed. In these cases, all variable payments under the contract are accounted for as variable lease payments under ASC 842.

Resources: Section 4.4 of KPMG's Handbook, Leases; KPMG's web article; ASU 2018-11

Proposed narrow-scope improvements for lessors

The FASB's proposed amendments would:

- add a practical expedient permitting lessors to present collections of sales and other similar taxes that arise from a specific lease transaction net of the lessor's payment of such taxes; and
- require a lessor to present lessor costs and payments made by the lessee directly to a third party (e.g. an insurer) on a net basis when the lessor cannot readily determine the amounts paid by the lessee to the third party.
  - Lessor costs include property taxes on the underlying asset for which the lessor is the primary obligor, and insurance on the underlying asset required by the lease contract for which the lessor is the primary beneficiary.
  - This proposal might apply to lessor costs of insurance on the underlying asset when the lessee is the policy owner and is not required, nor expected, to report its premiums to the lessor, or insures the asset through an umbrella policy.

The proposed amendments would also clarify that:

— a lessor should allocate variable payments between the lease and non-lease components of a lease contract under the allocation guidance in ASC 606; and

— a lessor's timing of its revenue recognition of the portion of such payments allocated to ASC 606 non-lease components is also governed by the guidance in ASC 606.

The comment period ended September 12.

Resources: Sections 4.2 and 7.3 of KPMG's Handbook, Leases; KPMG's web article; Proposed ASU

Implementing the hedging standard

In the third quarter of 2017, the Board issued ASU 2017-12, Derivatives and Hedging (Topic 815), *Targeted Improvements to Accounting for Hedging Activities*. ASU 2017-12 essentially made it easier for Companies to attain hedge accounting. A lot of Companies within our industry have gone away from hedge accounting. The Board has two additional projects on its standard-setting agenda related to this standard. The main item that could impact the industry is related to a project to clarify whether a company can change the hedged risk and/or the hedged forecasted transaction during the term of the hedging relationship.

Separately, the Board met in September to discuss issues raised during implementation activities and related Codification amendments and expects to issue Codification improvements in the fourth quarter.

Resources: Issues In-Depth, Hedging – Targeted Improvements

FASB proposals on balance sheet debt classification

In August, the FASB redeliberated its proposed ASU on simplifying the balance sheet classification of debt and tentatively decided these issues:

— **Unused long-term financing arrangement.** A borrower would disregard an unused long-term financing arrangement in place at the balance sheet date when determining the classification of debt unless it is explicitly available to refinance an existing debt. The Board had previously decided that an existing unused long-term financing arrangement could support noncurrent presentation for current maturities of other debt arrangements. This change could impact member companies that issue remarketable debt, such as certain pollution control bonds.

— **Grace periods**. A borrower who violates a covenant for which there is a specified grace period to cure the violation would classify the debt as noncurrent. The borrower also would disclose the violation and information related to the grace period.

The new ASU would be effective for:

- **public companies** – For fiscal years, and interim periods within those fiscal years, beginning after December 15, 2020; and
- **all other entities** – For fiscal years beginning after December 15, 2021, and interim periods within fiscal years beginning after December 15, 2022.

The FASB expects to issue a final ASU in the fourth quarter

Resources: KPMG's Defining Issues, FASB proposes simplification to balance sheet classification of debt; Proposed ASU

Accounting for cloud computing arrangements

In August, the FASB issued ASU 2018-15 on a customer's accounting for implementation costs incurred in a cloud computing arrangement. Under the amendments, a company should defer implementation costs that it incurs if the customer would capitalize those same costs under the internal-use software guidance for an arrangement that is a software license. The amendments are effective for interim and annual periods in fiscal years beginning after December 15, 2019. Early adoption is permitted.

Resources: KPMG's Defining Issues, FASB issues ASU on accounting for implementation costs of cloud computing arrangements; ASU 2018-15

FASB updates the conceptual framework and issues amendments to the disclosure framework

In August, the FASB issued two changes to its Conceptual Framework.

- **New chapter on disclosures**. The new chapter describes the purpose of the notes to financial statements, the nature of appropriate content and the general limitations of disclosure. The chapter also includes considerations specific to interim reporting.
- **Updated definition of materiality.** The FASB aligned its definition of materiality with other definitions in the financial reporting system – i.e. the definition used by the SEC, the PCAOB, AICPA and the United States judicial **system**.

Resources: FASB Concepts Statement No. 8, Chapter 8, Notes to the financial statements; FASB Concepts Statement No. 8, Amendments to Chapter 3, Qualitative characteristics of useful financial information

In August, the FASB issued amendments to ASC 820, Fair Value Measurement, and ASC 715-20, Defined Benefit Plans. The amendments add, remove or clarify disclosure requirements.

- ASU 2018-13, Disclosure Framework – Changes to the Disclosure Requirements for Fair Value Measurement, is effective for all companies in fiscal years beginning after December 15, 2019 – i.e. 2020 for calendar year-end companies. Early adoption is permitted for all entities.

- ASU 2018-14, Disclosure Framework – Changes to the Disclosure Requirements for Defined Benefit Plans, is effective for public companies in fiscal years ending after December 15, 2020 – i.e. 2020 for calendar year-end public companies and all other entities in fiscal years ending after December 15, 2021. Early adoption is permitted for all entities.

Resources: KPMG's Defining Issues, FASB amends fair value disclosure requirements and FASB amends defined benefit plan disclosures; ASU 2018- 13; ASU 2018-14

Critical audit matters

Implementation of Phase 2 of the PCAOB's AS 3101 standard regarding communication of critical audit matters (CAMs) is quickly approaching. The effective dates are:

- for audits of large accelerated filers: fiscal years ending on or after June 30, 2019; and for audits of all other companies to which the requirements apply
- fiscal years ending on or after December 15, 2020.

Phase 2 requires auditors to report on the CAMs identified in the audit of the current period's financial statements. CAMs are matters that were communicated to the audit committee, relate to accounts or disclosures that are material to the financial statements and involved especially challenging, subjective or complex auditor judgment.

In the auditor's report, the auditor identifies the CAM and describes the:

- principal considerations in concluding it is a CAM;
- primary procedures performed to address the CAM; and
- relevant financial statement accounts or disclosures that relate to the CAM.

It is expected that in most audits, the auditor will identify at least one CAM. However, in the infrequent circumstances that no CAMs are identified, the auditor is required to state that in the auditor's report.

Early engagement between the auditor, management and audit committee will be key to successfully implementing the CAM reporting requirement.

Management and the audit committee should begin talking now with their auditor about potential CAMs and how their identification and descriptions compare with information currently disclosed by the company.

While the standard does not prohibit the auditor from providing original information in its report, it should limit that information to describing the principal considerations in concluding that a matter was a CAM and how it was addressed in the audit.

Resources: CAQ publication - Critical Audit Matters: Key Concepts and FAQs for Audit Committees, Investors, and Other Users of Financial Statements; PCAOB Standard and Related Amendments

Projects and Agenda Priorities

Disclosure framework

In July, the FASB discussed the staff's approach to the interim disclosures reporting project. The FASB directed the staff to develop principles for interim disclosures and to perform research and outreach.

Improving the accounting for asset acquisitions and business combinations

In May, the FASB discussed Phase 3 of the Definition of a Business Project: Improving the Accounting for Asset Acquisitions and Business Combinations. The Board discussed how certain areas within the accounting for asset acquisitions and business combinations could be aligned, specifically contingent consideration, in-process research and development and acquisition costs. No technical decisions were made at the meeting.

Segment reporting

In June, the FASB staff discussed with the Board a plan to undertake extended outreach on the segment reporting project. The extended outreach would focus on two alternatives:

— re-ordering the process for determining reportable segments and move the quantitative thresholds earlier in that process; and

— removing the aggregation criteria so that each operating segment would be reportable until a practical limit is reached.

The FASB began its extended outreach in August.

Recent EEI & AGA Trainings and Other Events

Lease Workshop

AGA and EEI along with Deloitte held a workshop in September that helped participants understand the logic, implications, problem areas and major changes around lease accounting for power and utility companies. Topics covered include: lease definition, components and key concepts; power and utility contracts and issues; lessee accounting; lessor accounting; key implementation issues, diagnostics, and best practices; interactions with current GAAP including ASC 980; and presentation, disclosures and transition. The workshop was attended by 100 industry professionals.

Derivatives and Hedge Accounting Workshop

AGA and EEI along with EY held a workshop in September that walked participants through the derivatives and hedging standard and to discuss recent changes to hedge accounting. The workshop was attended by 85 industry professionals.

FERC Accounting & Reporting Workshop

AGA and EEI along with Deloitte held a workshop in September that walked participants through FERC accounting and reporting requirements. The workshop was attended by 111 industry professionals.

Public Utility Training Courses

EEI and AGA conducted their annual industry training program in August which includes the following courses:

- Utility Internal Auditor's Training Course
- Introduction to Public Utility Accounting Course
- Advanced Public Utility Accounting Training Course

The courses are taught by expert utility instructors and respected leaders in the field. The accounting courses cover the fundamentals of the utility business and public utility accounting, as well as more complex and specific advanced accounting and industry topics plus timely accounting issues. The audit course consists of a wide range of audit topics in areas affecting the regulated utility, competitive business operations, information technology and corporate services. The training program was attended by 225 industry professionals.

AGA Accounting Principles Committee Meeting

AGA conducted its annual Accounting Principles Committee meeting in August. The courses and topics were taught by expert utility instructors and various members of the Big 4, FASB and industry professionals. The topics discussed included updates on FASB, SEC and PCAOB guidance, statement of cash flow preparation and industry updates.

Upcoming EEI & AGA Accounting Committee Events

Below is a summary of upcoming accounting related events (joint AGA-EEI meetings unless indicated otherwise)

November 11-14, 2018	San Antonio, TX	Fall Accounting Conference
November 14-15, 2018	San Antonio, TX	Property Accounting and Depreciation Training Seminar
May 19-22, 2019	Nashville, TN	Spring Accounting Conference
June 2-5, 2019	Newport, RI	AGA Taxation Committee Meeting
June 23–26, 2019	Newport, RI	AGA/EEI Accounting Leadership and Chief Audit Executives Conference
August 11-14, 2019	TBD	AGA Accounting Principles Committee
August 19-22, 2019	Cleveland, OH	Public Utility Accounting & Auditor Training Courses