EEI & AGA Executive Accounting News Flash

June 2019

Dear Colleagues:

Although calendar year-end public companies cleared the first hurdle of adopting the leases standard, more work remains. Companies still are asking questions about applying the standard and are required to provide all of the disclosures that apply for annual periods each quarter during the year of adoption.

The FASB continued its efforts to clarify and address implementation issues associated with the financial instruments standards. Of note, the FASB issued Codification improvements affecting all three of those standards (credit losses, derivatives and hedging, and recognition and measurement).

Meanwhile, the SEC staff remains dedicated to its simplification and disclosure initiative. Recent SEC efforts include a new rule that amends certain Regulation S-K disclosure requirements and a proposal that would simplify disclosures about business acquisitions and dispositions. In response to an SEC request, the FASB also issued a proposed ASU that would incorporate certain SEC disclosure requirements into US GAAP.

Also during the quarter, new requirements directing auditors to identify critical audit matters in the auditor's report became effective for audits of large accelerated filers.

Herein, we summarize these and other accounting and financial reporting developments potentially affecting you in the current period or near term.

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Current quarter financial reporting matters

Leases – Adoption-year reminders

Calendar year-end public companies were required to adopt the new leases standard (ASC 842) in the first quarter of 2019. All other public companies are required to adopt ASC 842 on the first day of their fiscal year that begins during 2019. Private companies are required to adopt the standard in 2020.

Annual disclosures required in interim periods

Article 10 of Regulation S-X requires SEC registrants to provide the annual and interim disclosures required by a new accounting standard in each quarterly report in the year of adoption – i.e. for ASC 842, the first, second and third quarter Form 10-Q filings during 2019.

Disclosures for comparative periods

A company that adopts ASC 842 using the effective date transition method (i.e. effective date = date of initial application):

— is not required to provide ASC 842 disclosures in comparative periods, but

— is required to include disclosures previously required or otherwise provided under ASC 840 for that comparative period, including interim periods.

While companies typically did not include operating and capital lease commitment tables in their interim financial statements under ASC 840, companies that adopt ASC 842 using the effective date transition method should include their final operating and capital lease commitment tables as of the last balance sheet date presented under ASC 840 (e.g. December 31, 2018 for a calendar year-end public company) in each quarterly and annual report during the year of ASC 842 adoption.

Presenting new lease-related deferred tax assets and liabilities

On adopting ASC 842, lessees will record significant new deferred tax assets and liabilities arising from the newly recognized ROU assets and lease liabilities for ASC 840 operating leases. Lessees should present these new deferred tax assets and liabilities net for each tax jurisdiction on the balance sheet, but must present those items gross in their income tax disclosures.

KPMG resources: KPMG's webpage on Leases; Handbook: Leases; and Handbook: Statement of cash flows (Chapter 14, Leases – Topic 842)

SEC headlines

SEC amends Regulation S-K disclosures

The SEC issued a final rule that amends Regulation S-K to:

- streamline and simplify disclosures;
- modernize rules that had not been recently updated; and
- leverage technology to enhance investors' access to information.

Among the changes, registrants will be allowed to omit confidential information from most exhibits without filing a confidential treatment request. The rule also allows registrants some flexibility in discussing historical periods in Management's Discussion and Analysis. Specifically, the rule:

1. eliminates reference to the five-year selected financial data for trend disclosures; and
2. limits the periods covered to the two most recent fiscal years presented in the financial statements if the earliest year was included in a prior filing.

Companies electing not to include the earliest year must clearly identify where the omitted disclosure appeared in a prior filing. They also are required to provide hyperlinks to information (e.g. prior filings) incorporated by reference.

SEC proposes changes to disclosures about acquired and disposed businesses

As part of its disclosure effectiveness initiative, the SEC issued a proposed rule that would improve the information investors receive about business acquisitions and dispositions. Among other things, the proposed rule would:

- update the significance tests by:
  - revising the investment test and income test;
  - expanding the use of pro forma financial information in measuring significance; and
  - conforming the significance threshold and tests for a disposed business.
- require up to two (versus three) of the most recent fiscal year financial statements of the acquired business;
- clarify when financial statements and pro forma financial information are required;
- eliminate the requirement to provide separate acquired business financial statements when the business has been included in the registrant's post-acquisition financial statements for a complete fiscal year;
- align the Rule 3-14 requirements for acquisitions of significant real estate operations to Rule 3-05 when no unique industry considerations exist; and
- improve the content and relevance of pro forma financial information.

EEI and AGA are considering issuing a comment letter on this proposed rule. The comment period ends July 29.

KPMG resources: KPMG's Defining Issues, SEC proposes changes to disclosures about acquired and disposed businesses

The effective date for CAMs is here

Implementation of Phase 2 of PCAOB AS 3101 about communication of critical audit matters (CAMs) by auditors is effective:

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

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

The auditor identifies the CAM in the auditor's report and describes the:

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

The PCAOB expects that in most audits, the auditor will identify at least one CAM. However, in the infrequent circumstance in which no CAMs are identified, the auditor is required to state that in the auditor's report.

Ongoing engagement between the auditor, management and the audit committee will be key to successfully implementing the CAM requirements. Management and the audit committee should talk with their auditor about potential CAMs, including how the specific matters and related descriptions compare with information that the company already discloses.

It is not expected that the auditor would provide information in its report about the company that has not been made publicly available by the company, unless that information is necessary to describe the principal considerations in concluding that a matter was a CAM and how it was addressed in the audit.

External resources:

PCAOB staff guidance: Implementation of Critical Audit Matters: The Basics, Implementation of Critical Audit Matters: Staff Observations from Review of Audit Methodologies, Implementation of Critical Audit Matters: A Deeper Dive on the Determination of CAMs, and Implementation of Critical Audit Matters: A Deeper Dive on the Communication of CAMs

CAQ publications: Critical Audit Matters: Lessons Learned, Questions to Consider, and an Illustrative Example and Critical Audit Matters: Key Concepts and FAQs for Audit Committees, Investors, and Other Users of Financial Statements

New standards and guidance

Amendments to the credit losses standard

The FASB has been devoting attention to its financial instruments projects, particularly on finalizing amendments to the credit losses standard (ASU 2016-13), which becomes effective for many public companies in 2020.

Targeted transition relief

ASU 2019-05 allows companies to irrevocably elect the fair value option for existing financial assets on an instrument-by-instrument basis on adoption of ASU 2016-13. Except for existing held-to-maturity debt securities, the alternative is available for all instruments in the scope of ASC 326-20 that are eligible for the fair value option in ASC 825-10. If a company elects the fair value option, it will recognize as a cumulative-effect adjustment the difference between the fair value of the instrument and its carrying amount.

KPMG resources: KPMG's Defining Issues, FASB provides guidance on recoveries and extension options under credit losses standard

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Credit losses – Implementation issues for public companies

As public companies gear their efforts toward implementing the credit losses standard, they must ensure that they satisfy the disclosures required under SAB Topic 11.M (SAB 74) and that their audit committees allocate time and attention to the company's financial reporting before the adoption date.

SAB 74 disclosure reminders

SAB 74 requires public companies to disclose the potential effects of adopting an accounting standard before it is adopted, unless the effects are not expected to be material. Companies should consider disclosing qualitative and quantitative information and indicate their progress toward implementation. If a company cannot reasonably estimate the effect, it should consider providing additional qualitative disclosures.

The SEC staff has stated that it expects disclosures about adopting a new accounting standard to become increasingly more informative as the effective date approaches. **This standard is not expected to have a material impact to the companies within the industry.**

KPMG resources: KPMG's Hot Topic, Credit impairment: Disclosures required before adoption

Projects and agenda priorities

Incorporating certain SEC disclosure requirements into US GAAP

The FASB issued a proposed ASU that would incorporate several SEC disclosures and presentation requirements into US GAAP. The proposal also would introduce new disclosure requirements for private and not-for-profit entities.

Other disclosures would be required for public companies only, similar to existing SEC requirements. Public companies would be required to move certain disclosures from Management's Discussion and Analysis into the audited financial statements.

The proposals are the FASB's response to an SEC request that the Board consider incorporating into the Codification certain SEC disclosure requirements that overlap with but provide incremental information to US GAAP.

KPMG resources: KPMG's web article

Renewed attention on income taxes

With tax reform in the rearview mirror, the FASB revisited its disclosure and simplification projects on income taxes.

Amending income tax disclosures

As part of its disclosure framework project, the FASB re-proposed an ASU that would modify, eliminate and add income tax disclosures. The FASB first proposed an ASU in July 2016, but revised several of its proposals based on stakeholder feedback and the effects of US tax reform.

In a scoping decision that would affect all ASC 740 disclosures, the FASB proposed to replace the term 'public entity' with the term 'public business entity' (PBE). If an entity is not considered a public entity but meets the definition of a PBE, it would be subject to all the PBE disclosure requirements.

Among the proposals, **all companies** would be required to:

— disaggregate income (or loss) from continuing operations before intra-entity eliminations between domestic and foreign; and

— disaggregate income tax expense (or benefit) from continuing operations and income taxes paid between federal or national, state and foreign.

The comment period ended May 31. EEI/AGA filed a joint comment letter on May 31 generally supportive of the proposed rules while highlighting certain aspects with which we disagreed.

KPMG resources: KPMG's Defining Issues, FASB re-proposes changes to income tax disclosures

Simplifying income tax accounting

As part of its simplification initiative, the FASB issued a proposed ASU that would remove certain exceptions from and add new guidance to ASC 740 (income taxes) to reduce complexity.

Among other things, the proposals would eliminate the exceptions that currently require a company to:

— consider gains reflected outside of continuing operations when allocating total income tax expense or benefit to a loss in continuing operations;

— continue to recognize a deferred tax liability related to its outside basis difference for a foreign investment when it transitions from the equity method to consolidation; and

— continue to not recognize a deferred tax liability related to its outside basis difference for a foreign investment when it transitions from consolidation to the equity method if it has historically applied the indefinite reversal criterion.

The proposals would simplify income tax accounting by requiring companies:

— that pay a franchise tax with an income tax component to first account for the income tax component under ASC 740 and then account for incremental non-income-based tax as incurred; and

— in their interim period calculations, to (1) reflect a change in tax law in the estimated annual effective tax rate in the period of enactment, and (2) recognize the tax benefits of a year-to-date loss regardless of whether that loss exceeds the anticipated annual loss.

The comment period ended June 28. EEI/AGA are evaluating whether to submit a joint comment letter supporting the Board's view which allows companies the option to allocate taxes to single member LLC's. This will be important for our industry, particularly for rate regulated LLCs.

KPMG resources: KPMG's web article

Hedge accounting developments

With respect to hedge accounting, the FASB has on its agenda:

— a narrow-scope project about the 'last-of-layer method', specifically, how to account for the basis adjustments and multiple-layer hedging strategies;

— a Codification improvement project that includes clarifying whether a company can change the hedged risk and/or the hedged forecasted transaction during the term of the hedging relationship; and

— a project to address the effects on financial reporting of the market-wide migration away from interbank offered rates (e.g. LIBOR) to alternative reference rates.

Also during the quarter, the FASB issued ASU 2019-04, which made targeted Codification amendments to all of its financial instruments standards, including ASU 2017-12.

KPMG resources: KPMG's webpage on Financial instruments

FASB adds new topics to EITF agenda

At its June 13 meeting, the Emerging Issues Task Force (EITF) will discuss the following issue added to its agenda and stakeholder feedback on a proposed ASU.

— Financial instruments—Clarifying the interactions between ASC 321 (equity securities) and ASC 323 (equity method and joint ventures); and

Utility Industry Accounting Fellowship Succession

Rob Wilson was recognized at the Accounting Leadership Conference for his service as the Utility Industry Accounting Fellow, and his term will conclude at the end of September. Leadership of the AGA Accounting Leadership Council and the EEI Accounting Executive Advisory Committee, supported by leaders of each association's technical accounting committees, interviewed candidates for the next two-year Fellowship term beginning October 1. Upon conclusion of the interviews, Conor Tamms of Deloitte was selected to serve as the next Fellow. Rob Wilson will continue to serve in this role through the end of his term in September and assist in the transition.

Recent EEI & AGA Trainings and Other Events

Accounting Leadership and Chief Audit Executive Conference

The EEI and AGA conducted their annual accounting leadership and chief audit executives conference in Newport, RI from June 23rd through June 26th, highlighted by remarks from FASB Vice Chair Jim Kroeker, PCAOB Board Member Duane DesParte, and FERC Chief Accountant Steven Hunt. Topics covered included: current energy issues facing Boards of Directors, FASB/SEC/PCAOB update, FERC update, perspectives of Wall Street, fraud, cybersecurity and data & analytics. The conference was attended by 125 Chief Accounting Officers and Chief Audit Executives.

Upcoming EEI & AGA Accounting Committee Events

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

Date	Location	Event
August 11-14, 2019	Denver, CO	AGA Accounting Principles Committee
August 19-21, 2019	Cleveland, OH	Utility Internal Auditor's Training Course
August 19-22, 2019	Cleveland, OH	Introduction to Public Utility and Advanced Public Utility Accounting Training Course
September 17, 2019	St. Louis, MO	FERC Accounting and Reporting Workshop
November 17-20, 2019	Las Vegas, NV	AGA/EEI Tax Committee Meeting
November 17-20, 2019	Tucson, AZ	Fall Accounting Conference
November 20-21, 2019	Tucson, AZ	Property & Depreciation Accounting Training