

## Heads Up

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## Private Eyes

# FAF Establishes PCC to Watch Over Private-Company Standard Setting

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On May 23, 2012, the board of trustees of the Financial Accounting Foundation (FAF), the FASB's parent organization, approved the formation of the Private Company Council (PCC), which is tasked with improving the accounting standard-setting process for private companies. Shortly thereafter, the FAF released a [final report](#) discussing the establishment of the PCC and highlighting its two main responsibilities: (1) to determine whether exceptions or modifications to existing nongovernmental U.S. GAAP would benefit end users of private-company financial statements and (2) to advise the FASB on how private-company accounting matters should be treated on the FASB's technical agenda. Any modifications or exceptions to U.S. GAAP developed by the PCC (based on a two-thirds majority vote of its members) will become final if endorsed by the FASB.

### Background

Since its inception, the FAF has worked to ensure that:

- The FASB and GASB develop high-quality accounting standards that provide key, comparable financial statement information to investors, lenders, and other financial statement end users about companies, not-for-profit organizations, governmental bodies, and other entities that are required to file financial statements.
- Enacted standards reflect constituents' financial information needs and that implementation takes into account relevance, complexity, and costs versus benefits.

The FAF's effort to reconcile these objectives is ongoing; one of its greatest challenges is to address the needs of private companies. Many factors need to be considered. For example, end users of public-company financial statements often require different information than those of private-company financial statements. In addition, a "one size fits all" approach to standard setting can put a strain on private companies, which often lack resources for proper implementation.

**Editor's Note:** The term "private company" is not uniformly defined in U.S. GAAP, and the FAF's final report does not specify which entities would be within the PCC's purview. We expect the PCC to clarify this important issue when it commences its activities.

## The Pathway to Creating the PCC

Over the years, the FAF and FASB have worked to better understand the concerns of preparers and users of private-company financial statements. According to the FAF's report, "no fewer than 12 separate reports, studies, or formal recommendations on issues related to private companies [have been] produced, with varying degrees of impact and success."

The efforts of the FAF and FASB to address private-company standard setting have included the FASB's creation of the Private Company Financial Reporting Committee in 2006 and the FAF's nationwide listening tour in 2009. Other actions taken to improve standards for private companies have included the following:

- In 2010, creation of the Blue-Ribbon Panel on Standard Setting for Private Companies to assess and understand the needs of private-company financial statement users.
- In January 2011, issuance of the Blue-Ribbon Panel report, which contains recommendations for improving private-company standard setting.
- In March 2011, the convening of a "working group" to gather input from various other stakeholders.

As a result of these efforts, the FAF issued its initial proposal *Plan to Establish the Private Company Standards Improvement Council* in October 2011. (For more information, see Deloitte's October 10, 2011, *Heads Up*.)

## FAF Outreach on Initial Proposal

The FAF reached out to various stakeholders affected by private-company standard setting to get their views on the proposal. In October and November 2011, the FAF also presented an hour-long educational session, *In Focus: The FAF Plan to Improve Private Company Financial Reporting*. Further, after the close of the comment letter period on the initial proposal, the FAF hosted four separate roundtables at different locations to obtain additional feedback from various constituents, including users, preparers, auditors, regulators, and academics. As a result of its outreach, the FAF received more than 7,000 comment letters. Respondents included the AICPA, financial statement users and preparers, CPA firms, state CPA societies, state boards of accountancy, and other groups.

## Overview of the PCC, Operating Procedures, and Oversight

### PCC Membership and Term Limits

The FAF trustees will appoint 9 to 12 members to the PCC, including a chairman (who cannot be a FASB member) and one or more vice-chairmen. PCC members will need to have private-company experience and will represent various groups, including users, preparers, and auditors. Each council member will initially serve a three-year term but could be reappointed for a subsequent two years. The tenure of the council members may be staggered to provide continuity and stability while allowing for an orderly transition when new members are appointed.

**Editor's Note:** The initial proposal indicated that the council would consist of 11 to 15 members and include a chairman that would be a FASB member. However, the FASB ultimately decided, on the basis of feedback from constituents, that a smaller group of 9 to 12 members would be more effective. In addition, to limit the FASB's influence on the PCC, the FAF decided that the chairman would **not** be a sitting FASB member but would be independent from the FASB. Nevertheless, as with other FASB groups, a FASB member will be appointed as a liaison to the PCC.

PCC members will need to have private-company experience and will represent various groups, including users, preparers, and auditors.

The PCC will hold at least five meetings a year during its first three years of operations and may schedule additional meetings if necessary.

## FASB Liaison and FASB Staff Support

The goal of the FASB liaison will be to foster communication between the PCC and the FASB, ultimately improving the efficiency of the standard-setting process. Further, the FASB will assign members of its administrative and technical staff to work directly with the PCC and will supplement the staffing of the PCC with other individuals with specific technical expertise when warranted.

## Agenda Setting

The PCC and FASB will work together to develop a decision-making framework for identifying suitable criteria for determining whether and, if so, when exceptions or modifications to U.S. GAAP are warranted for private companies. On the basis of these criteria, the PCC will set its agenda by considering existing U.S. GAAP to determine when exceptions or modifications may be appropriate. Agenda items will be determined by a two-thirds majority vote after the PCC consults with FASB members and analyzes input from other affected stakeholders.

Initially, the PCC is expected to focus only on existing standards for which modifications or exceptions may be appropriate for private companies. Because the PCC will be working with and advising the FASB on projects currently under consideration, the PCC will not add any of these same projects to its own agenda.

**Editor's Note:** While the initial proposal did not include guidance on "agenda setting," feedback indicated that the new council should be able to create its own agenda. While views were mixed regarding the extent to which the FASB should be involved in establishing the agenda, the FAF ultimately concluded that the PCC should have the power to establish its own agenda in consultation with the FASB and other stakeholders.

## Process for Voting for Exceptions/Modifications and FASB Endorsement

Using the aforementioned decision-making framework and related criteria, the PCC will review existing U.S. GAAP to identify standards for which exceptions or modifications might be warranted for private companies. The PCC will then develop, deliberate, and vote on proposed exceptions or modifications. Upon approval by a two-thirds majority of the PCC, the proposed exceptions or modifications will be initially subject to FASB endorsement (a simple majority vote of FASB members), after which they will be exposed for public comment.

After the comment period, the PCC will redeliberate the proposed exceptions or modifications and submit the final proposal to the FASB for final endorsement, which will generally be made within 60 days. If endorsed, the modification or exception will be incorporated into existing U.S. GAAP. If the FASB does not endorse the proposed exception or modification, the FASB chairman must submit a written explanation (that will be part of the public record) detailing the reasons why as well as possible changes that could result in FASB endorsement.

## Meetings

The PCC will hold at least five meetings a year during its first three years of operations and may schedule additional meetings if necessary. Most meetings will be held at the FAF's offices in Norwalk, Connecticut; however, up to two meetings each year may be held at an alternative location. Deliberative meetings will be open to the public and must be attended by all FASB members; at least two-thirds of the PCC members must be present to constitute a quorum. Administrative and educational meetings may be closed to the public; the PCC chairman has the discretion to hold these closed meetings without any FASB members in attendance. According to the FAF report, "[n]o more than three FASB members may attend closed educational or administrative meetings of the PCC that address technical matters."

**Editor’s Note:** In response to feedback obtained during the outreach process, the FAF decided to allow the PCC to hold closed sessions without FASB members present.

After the first three years of operations, the FAF trustees will assess the PCC to determine whether its overall objectives are being met or whether additional changes to the private-company standard-setting process are needed.

## Oversight

The FAF’s board of trustees will establish a Private Company Review Committee (the “Review Committee”) that is chaired by a trustee who has significant experience with private-company accounting matters. This committee will be tasked with overseeing the PCC for an initial three-year period and will strive to ensure that private-company issues are considered during the standard-setting process. The PCC and FASB will be held accountable by the committee if this objective is not achieved.

During this three-year period, the PCC will provide in-person and written periodic reports to the Review Committee. In addition, the PCC will be required to submit quarterly reports to the full FAF board of trustees.

## FAF Three-Year Assessment

After the first three years of operations, the FAF trustees will assess the PCC to determine whether its overall objectives are being met or whether additional changes to the private-company standard-setting process are needed. In addition, after this period, the Review Committee’s responsibilities are expected to be transitioned to the existing Standard-Setting Process Oversight Committee of the Trustees.

## What’s Next for the PCC?

Now that the FAF has formally approved the establishment of the PCC, the next step will be to appoint members, the chairman, and vice-chairmen (if deemed necessary). Once the PCC is formed, the PCC and FASB are expected to finalize the aforementioned decision-making framework.

In addition, on June 1, the FAF trustees issued a [Request for Nominations to the FAF’s Private Company Council](#) soliciting nominations for the chairman and members to serve on the council. The FAF trustees will consider individuals with varying backgrounds and experience, including preparers, auditors, and users of private-company financial statements. Completed nomination forms and supporting information should be submitted to the FAF by June 30. Further, on June 28, the FASB will hold a [webcast](#) on, among other topics, the establishment of the PCC by the FAF.

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