



# Defining Issues<sup>®</sup>

## SEC staff comments on implementation of new accounting standards

September 28, 2017

KPMG reports on the SEC staff's observations about adoption of the new revenue, leases and credit losses standards.

### Applicability

All SEC registrants adopting ASC 606, *Revenue from Contracts with Customers*; ASC 842, *Leases*; and ASC 326, *Financial Instruments – Credit Losses*.

### Key facts and impacts

In a recent speech on accounting change,<sup>1</sup> SEC Deputy Chief Accountant Sagar Teotia made several observations related to the adoption of the new revenue, leases and credit losses standards.

- Now is the time to make implementation efforts a priority.
- Internal controls over financial reporting will most likely change and require time to implement.
- The SEC expects to see increasingly informative SAB 74 transition disclosures in the periods prior to adoption of the standards.
- New required disclosures are an important aspect of adoption and may be time consuming.
- The SEC is available for pre-filing consultations and will accept reasonable, thoughtful judgments.
- Audit committees set the tone for successful implementations and should be actively engaged.

Companies and their stakeholders should consider these observations and thoughtfully evaluate their current and planned implementation efforts for these major standards.

### The time is now

Many companies have made meaningful progress toward implementation of the new standards, but significantly more work remains to ensure that their efforts are successful. Implementations are time-consuming, and companies need adequate time to identify accounting questions, make reasonable judgments and implement effective internal controls. Companies are encouraged to engage in implementation efforts on these new standards concurrently rather than sequentially based on their effective dates.

### Internal controls over financial reporting

The new standards introduce accounting and disclosure requirements that will most likely result in new or different internal controls over financial reporting. It may be most efficient and effective in some areas for companies to evaluate and implement internal control changes concurrently with their evaluation and implementation of the new accounting and disclosure requirements.

<sup>1</sup> [Addressing Implementation Matters to Improve Financial Reporting](#), Sagar Teotia, SEC Deputy Chief Accountant, September 21, 2017

### **SAB 74 disclosures**

The SEC staff continues to focus on SAB 74 disclosures made by companies and expects companies to clearly communicate to financial statement users where they stand with their implementation efforts. The SEC staff expects SAB 74 disclosures to be increasingly informative in subsequent periodic filings and reminded companies that the assessment of whether a standard has a material effect on a company's financial statements must include consideration of the new disclosures that the standard requires.

### **New disclosures**

Companies must dedicate adequate time and resources to prepare for the new disclosures because it may be time consuming to make judgments, gather data and implement system or control changes to comply with the new requirements. Companies are at risk of falling behind if they have not begun work on the new revenue disclosures.

### **Reasonable judgment and SEC pre-filing consultations**

The SEC staff will continue to accept well-reasoned and thoughtful judgments in the application of the new standards. However, time is required to develop well-reasoned judgments. Companies must gather relevant facts and consider all accounting alternatives before making judgments or reaching conclusions. The SEC staff is available for both formal and informal consultations for all of the new standards. However, the SEC staff urges companies to ask questions now about the revenue standard so they avoid a backlog of consultations, which may not serve the best interests of stakeholders.

### **Audit committee responsibilities**

In the important role of overseeing management's efforts and the external audit process, audit committees are critical to setting the right "tone at the top" needed to successfully implement the new standards. Audit committees should actively monitor management's efforts and spend the necessary time to understand and assess the quality and status of their implementation efforts.

### **KPMG observation – Revenue**

Preparing disclosures, designing and implementing internal controls, and finalizing accounting conclusions continue to take much longer than companies anticipated. With only a few months before the effective date, revenue standard implementation efforts must be prioritized.

The SEC staff will particularly focus on SAB 74 disclosures for the new revenue standard in upcoming 10-Q and 10-K filings, and expects them to be highly informative and reflect the status of the company's implementation process. The SEC staff also expects to see a materiality assessment that encompasses all aspects of implementation, including internal controls and disclosures.

Companies should not wait to engage their audit committees, external auditors or the SEC staff on their difficult accounting judgments. The volume of consultations within accounting firms and with the SEC is expected to increase as the deadline approaches. Companies that delay these discussions may not give themselves, their audit committees or external auditors enough time to reach appropriate accounting conclusions in difficult areas of judgment before the adoption deadline.

## KPMG observation – Leases

While many companies have rightly dedicated resources to, and focused more of their attention on, the implementation of the revenue standard, management teams should not lose sight of the amount of time and effort the leases standard implementation may require.

Getting started now, rather than waiting until revenue implementation efforts are completed, with lease identification, impact assessments and design and implementation of new processes and controls will reduce surprises and increase implementation quality. For example, new processes and controls to identify lease modifications and events that will trigger reassessments or impairments may need to be designed and implemented.

Giving renewed focus to current lease disclosures<sup>2</sup> as part of the current annual financial reporting cycle also has the potential to significantly help companies' implementation efforts. And even though the mandatory adoption date is one year later than the revenue standard, companies should similarly be engaging their audit committees now and should not wait to identify and consult with their external auditors and, potentially, the SEC staff on complex lease accounting issues.

## KPMG observation – Credit losses

The credit losses standard marks a significant accounting change for many companies and requires allocation of sufficient resources to adoption efforts. Companies should consider raising challenging interpretive questions to the Credit Losses Transition Resource Group and continue to monitor the implementation questions and emerging views coming out of that process.

## Effective dates and implementation resources

Revenue	Public business and certain other entities <sup>3</sup>	All other entities
Annual periods – In fiscal years beginning after	December 15, 2017	December 15, 2018
Interim periods – In fiscal years beginning after	December 15, 2017	December 15, 2019
Early adoption allowed?	Yes, for fiscal years beginning after December 15, 2016, including the interim reporting periods within that annual reporting period. <sup>4</sup>	
KPMG implementation resources	<a href="#">Handbook: Revenue recognition</a> <a href="#">Issues In-Depth: Illustrative disclosures</a> <a href="#">KPMG Executive View: ASC 606 implementation – don't forget internal controls and disclosures</a>	

<sup>2</sup> Those required by ASC Topic 840, Leases

<sup>3</sup> Certain other entities include (1) not-for-profit entities 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 (2) employee benefit plans that file financial statements with the SEC.

<sup>4</sup> All other entities may also choose to early adopt in interim reporting periods within the annual period subsequent to initial application.

Leases	Public business and certain other entities <sup>5</sup>	All other entities
Annual periods – In fiscal years beginning after	December 15, 2018	December 15, 2019
Interim periods – In fiscal years beginning after	December 15, 2018	December 15, 2020
Early adoption allowed?	Yes, immediately.	
KPMG implementation resources	<a href="#">Handbook: Leases</a> <a href="#">KPMG Executive View: ASC 842, Leases – Transition disclosures</a>	

Credit losses	Public business entities that are SEC filers <sup>6</sup>	All other entities
Annual periods – In fiscal years beginning after	December 15, 2019	December 15, 2020
Interim periods – In fiscal years beginning after	December 15, 2019	December 15, 2020 <sup>7</sup>
Early adoption allowed?	Yes, all entities can adopt Topic 326 for annual and interim periods in fiscal years beginning after December 15, 2018.	
KPMG implementation resources	<a href="#">Issues In-Depth: Credit impairment</a>	

<sup>5</sup> Certain other entities include (1) not-for-profit entities 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 (2) employee benefit plans that file financial statements with the SEC.

<sup>6</sup> An SEC filer is an entity that is required to file or furnish its financial statements with either (a) the SEC or (b) with respect to an entity subject to Section 12(i) of the Securities Exchange Act of 1934, as amended, the appropriate agency under that Section. Financial statements for other non-SEC filers whose financial statements are included with another filer’s SEC submission are not included in this definition.

<sup>7</sup> For non-public business entities, including not-for-profit entities, and employee benefit plans within the scope of ASC 960, Defined Benefit Pension Plans; ASC 962, Defined Contribution Pension Plans; and ASC 965, Health and Welfare Benefit Plans, the standard is effective for annual periods in fiscal years beginning after December 15, 2020 and interim periods in fiscal years beginning after December 15, 2021.

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## KPMG’s Financial Reporting View

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