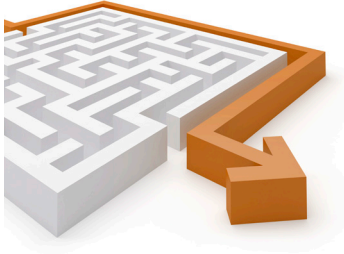


Private Company Financial Reporting



Overview

During 2010, the Blue Ribbon Panel on Private Company Financial Reporting – consisting of a cross-section of financial reporting constituencies, including lenders, investors, owners, preparers and auditors – explored the changes necessary to best meet the needs of U.S. users of private company financial statements. In January 2011, the panel – which the AICPA, the Financial Accounting Foundation (FAF, which oversees the Financial Accounting Standards Board and the Governmental Accounting Standards Board) and the National Association of State Boards of Accountancy sponsored – finalized its recommendations on the future of standard setting for private companies and submitted a report to the FAF. FAF Trustees discussed the report at a meeting in February 2011 and formed a Trustee Working Group in March to address accounting standard setting for nonpublic entities and gather public input.

It's critically important that CPAs, their private company clients, small businesses and their financial statement users – especially bankers/lenders, sureties and insurers, and venture capitalists – take action and help effect the historic change needed in financial reporting. The time to shape the outcome is now.

Recommended Changes

The two most significant Blue Ribbon Panel recommendations are that:

- A new, separate board with standard-setting authority be established under the oversight of the FAF. The board would coordinate activities with the FASB but not be subject to FASB approval.
- Changes and modifications be made to existing and future GAAP that recognize the unique needs of users of private company financial statements. All such changes would reside in the *FASB Accounting Standards Codification*[®].

Why This Effort Is So Important

Private companies play a vital role in our economy. There are about 29 million private and not-for-profit companies in the United States, including 7 million small- to medium-size businesses. CPAs who work for these companies, or who serve them, have been saying for a long, long time that these businesses have financial information needs that are much different from those of large public entities. Their financial statement users need straightforward, understandable information that addresses what they need to know – no more, no less. Given private

| March 1972 | March 1972 to February 2005 |
|-----------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------|
| <p><i>Report of the Study on Establishment of Accounting Principles, AICPA ("Wheat Report")</i></p> | <p><i>Numerous studies and reports on GAAP for private companies</i></p> |

companies' key role in job creation and economic development, it is more vital than ever that their financial statement users and other stakeholders, such as owners of those companies, have relevant and useful financial information.

AICPA's Position on Panel's Main Recommendations

The AICPA supports the panel's main recommendations that change in financial reporting for private companies is long overdue and that a separate, autonomous standard-setting body is necessary for effective private company reporting to become a reality.

Separate Board Is Critical for Effective Private Company Accounting Standards

Years of studies and research, a joint advisory committee with the FASB (i.e., the Private Company Financial Reporting Committee), private company constituent representation on the FASB board and comment letters on proposed accounting standards in the past have not yielded meaningful results. The AICPA believes it is imperative that there be a board made up of private company constituents who would set the different

standards affecting the private company financial reporting system. As it stands now, issues affecting public companies are what drive accounting standards and impact how they are written.

Private Company Financial Statement Users Agree Change Is Needed

Many constituents - including lenders, investors and owners - question the relevance and usefulness of a number of current GAAP standards as they relate to private companies. In fact, the Blue Ribbon Panel listened to users at its very first meeting and this group was also represented on the panel. Users appreciate that certain standards need to change to bring balance to the cost-benefit equation.

Examples of Standards Not Appropriate for Private Companies

The standard formerly known as FIN 48, on uncertainty in income taxes, is an excellent example, one that many CPAs and companies have wrestled with. In this case, and many others, the standard was created because of issues in public company reporting and the related regulatory oversight that accompanies it. Private company financial statement users



| February 2005 | May 2005 | June 2006 |
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| <p><i>Private Company Financial Reporting Task Force Report, AICPA ("Castellano Report")</i></p> | <p>AICPA Council directs AICPA management to work with FAF and FASB to explore GAAP for private companies</p> | <p><i>Invitation to Comment, Enhancing the Financial Accounting and Reporting Standard-Setting Process for Private Companies, FASB</i></p> |



find the accounting matters and disclosures encompassed by FIN 48 to be largely irrelevant to their purpose and decision-making activities.

FIN 46R, on consolidation of variable interest entities, is causing numerous unnecessary challenges for private companies. It was created because some public companies found loopholes in the old standards that they were able to work to their advantage. But private companies do not have similar incentives and pressure to game the system for investors. Still, they are now forced to consolidate common controlled structures that may have been created for tax purposes. This causes so many problems in private company financial statements that we often hear about lenders accepting GAAP exception audit reports so the company can issue a more relevant statement and sidestep FIN 46R altogether. The growing use of such exceptions weakens the relevancy of GAAP.

The rules on goodwill impairment force private companies to assess goodwill assets in business combinations for impairment annually, no matter what the circumstances. To comply, private companies often must perform calculations based on extensive, complicated fair value estimates. And yet, the users of private company financial statements

often say they totally ignore goodwill. It's clear that private companies are spending a great deal of time and money developing information that may never actually be used.

Cost Also Is a Factor for Change

CPAs are aware that U.S. GAAP has become exceedingly complex as business has become complex. A lot of that complexity arises out of publicly traded companies and the role they play in the economy. Too much of what is included in current financial statements is not useful to private company owners, lenders and investors. As a result, not only is this unnecessary reporting not cost beneficial, it also can stand in the way of good business decision-making by complicating the financial statements with data that are irrelevant to the analyses of most private company financial statement users.

Shape the Future of Private Company Financial Reporting

The FAF places a lot of importance on the amount of interest in a subject, the diversity of stakeholders represented and the input from certain critical groups relevant to particular issues. Make your voice heard.

| January 2007 | October 2009 | December 2009 |
|--------------------------------------------------------------------|-----------------------------------------------------------------------------------------|----------------------------------------------------------------------|
| AICPA and FASB start Private Company Financial Reporting Committee | AICPA Council expresses overwhelming support for GAAP differences for private companies | AICPA Council, FAF and NASBA announce formation of Blue Ribbon Panel |

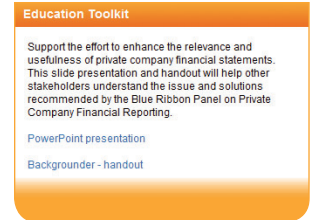
Write a letter to FAF and make three points:

- There is a systemic problem that has not been fixed despite decades of attempts.
- Significant differences to the standards within GAAP are necessary to recognize the unique needs of private companies and their financial statement users.
- A new separate standard-setting body needs to be created that would report directly to the FAF and not be subject to the FASB's approval. Emphasize that the separate board is essential to having effective private company financial reporting for the long run.

It is best if you write your own letter conveying your point of view and experiences, but if you prefer assistance, you can customize a letter using the AICPA's letter-writing tool available at aicpa.org/privateGAAP.

You can provide additional support by educating other stakeholders and urging them to write letters as well. The letter-writing tool is available to everyone, and an education toolkit is accessible on the website to help you explain the issue.

For more information and resources, visit aicpa.org/privateGAAP.



| October 2010 | January 2011 |
|--------------------------------------------------------------------------|-----------------------------------------|
| AICPA Council adopts resolution supporting the work of Blue Ribbon Panel | Blue Ribbon Panel releases final report |