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The New Era of Differential Standards

Recent U.S. and global developments signal the end of "one size fits all" accounting standards.

During the past few months, the decades-old question "Should there be different accounting standards for different kinds of businesses?" has been answered with a definitive "yes." In this column, I'll summarize recent progress toward accounting standards that better accommodate diversity among businesses.

Private Company Council

As I explained in my July 2012 column, the distinction between "public" companies and "private" companies remains unclear. Yet the importance of this distinction for standards-setting purposes has never been more significant. On May 23, 2012, trustees of the Financial Accounting Foundation (FAF) voted unanimously to establish the Private Company Council (PCC). In doing so, the FAF, which is the parent of the U.S. Financial Accounting Standards Board (FASB), has paved the way for the introduction of significant differences in accounting standards between private companies and public companies in the United States.

With regard to differential standards, the PCC will be responsible for recommending changes to existing U.S. Generally Accepted Accounting Principles (GAAP). It will also be the primary advisory body to the FASB regarding private-vs.-public differences in future standards. The new Council is expected to have its first meeting before the end of 2012.

Private Company Decision-Making Framework

Before the FAF created the PCC, the FASB had already begun considering whether and how to incorporate practical expedients, exceptions, modifications, and/or effective-date deferrals for private companies into the Board's standards. On July 31, 2012, it issued a discussion paper (DP) containing a draft of a *private company decision-making framework* that the Board and its staff are developing. The framework is intended for the FASB and the PCC to use to determine whether—and in what circumstances—to adjust the requirements of U.S. GAAP for private companies.

The development of this framework will ultimately identify:

- Differential information needs of users of public company financial statements and users of private company financial statements and
- Opportunities to reduce the complexity and costs of preparing financial statements in accordance with U.S. GAAP.

The DP also contains:

- Preliminary recommendations made by the FASB's staff with regard to differential recognition, measurement, disclosure, display (presentation), effective dates, and transition methods and
- A draft definition of a "nonpublic entity."

The discussion paper is available at the FASB's website (www.fasb.org). The deadline to submit comments on the paper is October 31, 2012.

An Alternative Framework

On the same day the FAF trustees voted to establish the PCC, the American Institute of Certified Public Accountants (AICPA) announced its plans to develop a financial reporting framework "to meet the needs of some privately held small- and medium-sized enterprises (SMEs) as well as the users of the financial statements of these entities." The AICPA has referred to the ultimate outcome of this initiative as an "OCBOA" framework, which is a reference to provisions of the Institute's Code of Professional Conduct that distinguish between GAAP and an "Other Comprehensive Basis of Accounting" that a company might use instead of GAAP to prepare financial statements. As the AICPA explains: "The SME OCBOA framework will be a less complicated and a less costly alternative system of accounting to U.S. GAAP for SMEs that do not need U.S. GAAP financial statements."

The AICPA has also referred to the ultimate outcome of this initiative as a "Financial Reporting Framework for Small- and Medium-sized Entities" (FRF for SMEs). According to the Institute, the FRF for SMEs will be a standalone, self-contained OCBOA intended for use by privately held SMEs in preparing their financial statements and will help SMEs meet the demand for financial statements that are prepared "in a consistent and reliable manner in accordance with a framework that has undergone public comment and professional scrutiny."

A separate initiative will help "micro-sized" entities.

FAF President Teresa S. Polley, responding to the AICPA's announcement, characterized the AICPA's initiative as "complementary" with regard to the FAF's decision to establish the PCC. "Taken together," Polley said, "these actions demonstrate the commitment of both organizations to the private company financial reporting constituency." The AICPA expects to publish its FRF for SMEs in early 2013.

Review of the IFRS for SMEs

While the preceding developments were occurring in the United States, the International Accounting Standards Board (IASB) continued its efforts to address similar issues from a global perspective. On June 26, 2012, the IASB issued a Request for Information (RFI) to launch its first comprehensive review of the International Financial Reporting Standard for Small and Medium-sized Entities (IFRS for SMEs), which the Board issued in July 2009. As the Board's press release indicated, "The objective of the Request for Information is to seek public views on whether there is a need to make any amendments to the IFRS for SMEs and, if so, what amendments should be made."

According to IASB member Paul Pacter, "Millions of small companies in around 80 jurisdictions are already using the IFRS for SMEs…This comprehensive review will enable the Board to fine-tune the Standard." Pacter's comments are a clear indication that the IASB believes the IFRS for SMEs has been successful and is here to stay. November 30, 2012, is the deadline for responses to the RFI, which is available at the IASB's website (www.ifrs.org).

Standards for the Smallest Entities

A month after issuing the RFI on the IFRS for SMEs, the IASB announced a separate initiative in which its staff will develop guidance to help "micro-sized entities" apply the standard. The Board's staff, aided by the Board's SME Implementation Group (SMEIG), will extract from the IFRS for SMEs the requirements that apply to most micro-sized entities. The extracted requirements wouldn't modify any recognition or measurement principles, so the guidance for micro-sized entities will be a proper subset of the IFRS for SMEs rather than a separate standard. This means that financial statements prepared in conformity with the micro-sized entities guidance would also conform fully to the IFRS for SMEs.

The IASB expects to publish the micro-sized entities guidance in early 2013. Like the AICPA's OCBOA project, the IASB's project for micro-sized entities reflects the growing perception among standards setters and their stakeholders that it's appropriate to make size-based distinctions among entities in addition to a simplistic public-vs.-private distinction.

As all these developments indicate, the era of "one size fits all" accounting standards is coming to an end. Accounting professionals in the United States and throughout the world can anticipate a future of differential standards that are better suited for the needs and capabilities of private companies, even the smallest ones. **SF**

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