Accounting, financial reporting, and regulatory developments

SECOND QUARTER 2022

In this update, we highlight some of the more important 2022 second quarter accounting, financial reporting, and regulatory developments that may impact both public and private companies. The content is not meant to be all-inclusive.

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Accounting guidance

Accounting guidance issued in second quarter 2022

ASU 2022-03, Fair Value Measurements (Topic 820): Fair Value Measurement of Equity Securities Subject to Contractual Sales Restrictions, provides updated guidance on determining the fair value of equity securities when those securities have contractual sales restrictions. The new ASU clarifies that a contractual sales restriction should not be considered when determining the fair value of the equity security. The new guidance also adds additional disclosure requirements for equity securities subject to contractual sales restrictions. The new ASU is effective for public business entities for fiscal years beginning after Dec. 15, 2023. For all other entities, the new guidance is effective for fiscal years beginning after Dec. 15, 2024.

New lease accounting standard effective for 2022

The FASB's new lease accounting standard, ASC Topic 842, will be effective for calendar year-end entities that have not previously adopted the new guidance for their 2022 annual financial statements. Many entities that have already adopted ASC Topic 842 have indicated the implementation process was more time-consuming than initially anticipated. Given this, entities that have not started working on their implementation efforts should look to get started as soon as possible in order to ensure a successful outcome. Some of the key steps for a successful implementation include:

- ***Forming an implementation team.*** *If entities have not already formed an implementation team, the first step should be to form one. While the implementation team is for the adoption of a new accounting standard, many organizations have found it necessary to include resources outside of the accounting/finance department on the implementation team. The implementation team should include team members responsible for negotiating and signing leases as well as members of the accounting/finance department. For entities with larger populations of leases, it may be necessary to include a member of the IT department to help assess technology solutions. Part of forming the implementation team should also include assessing resource needs so an entity can determine if it will be able to complete the implementation plan using internal resources, or if it will need to engage external resources to assist with the implementation.*

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- ***Creating and maintaining an inventory of leases.*** *Another important step to take early in the implementation process is to create and maintain an inventory of lease contracts. In organizations with few lease agreements and centralized processes for approving leases, this exercise may be relatively straightforward as leases may be maintained in a single location. However, in organizations where approval of leases is decentralized this may take additional work. While accounting departments are aware of the most significant leases, there may be leases that are individually insignificant but, in aggregate, become significant.*
- ***Assessing technology needs.*** *The new lease standard will require all leases (other than certain short-term leases as described below) to be recorded on the balance sheet. Organizations will need to assess how they will track and account for their leases. Options for tracking include use of spreadsheets, standalone lease software, and a lease accounting module for their enterprise resource planning (ERP) system. Each option has its advantages and disadvantages, and entities should evaluate which option best fits their needs based on the complexity of their lease population. Consideration should be given to the number of leases and complexity of the lease arrangements. Entities will also need to determine whether they plan to centralize the process of inputting leases into the chosen technology solution or if they plan to use a decentralized process for inputting leases. Entities should consider the technology solution they plan to employ as early as possible, so they are able to have the solution implemented prior to the end of the year. They will then be able to record the results of the implementation as part of the year-end close process.*
- ***Evaluating accounting policy elections and practical expedients.*** *The new lease standard allows entities to make accounting policy elections in a number of areas. It's important for entities to determine the accounting policy elections and practical expedients that will be used before entering leases into their technology solution. Some of the areas where entities can make accounting policy elections or elect practical expedients include:*
  - ***At transition:***
    - *Hindsight practical expedient — an entity may elect to use hindsight in determining the lease term*
    - *Package of practical expedients:*
      - *An entity need not reassess whether a contract contains a lease*
      - *An entity need not reassess lease classification determinations made under the previous lease standard*
      - *An entity need not reassess initial direct costs of existing leases*

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- » ***Ongoing:***
  - *Lessees may elect, by class of asset, not to separate lease and nonlease components. Entities would instead combine lease and nonlease into a single lease component.*
  - *Lessees may elect, by class of asset, to utilize the risk-free rate in place of the incremental borrowing rate (only available to private companies).*
    - » *Lessees may elect not to apply the recognition and measurement requirements to leases with a lease term of 12 months or less.*
    - » *Lessees may elect to account for leases at a portfolio level if the leases are entered into at or around the same time, and the resulting accounting would not be materially different from accounting for the leases if the election were not made.*
- ***Assessing debt covenant considerations.*** *Entities should also review existing contracts to determine if there may be impacts on covenants. While the impacts on covenants based on overall assets and liabilities are easily understood, some covenants may be based on debt service ratios or outstanding amount of debt. For these ratios, depending on how the covenant is written, payments on leases that are recorded on the balance sheet or the amount of the lease liability may impact these calculations. Affected entities should discuss covenant calculations with their lender prior to the adoption of the new standard if there is uncertainty as to how the new lease standard will impact the calculation. Entities and lenders may elect to amend covenants prior to the implementation of the lease standard to avoid potential covenant compliance issues.*

FASB drops project on subsequent accounting for goodwill

In June 2022, the FASB voted unanimously to remove its project on the subsequent accounting for goodwill. This ongoing project had been evaluating whether changes should be made to the subsequent accounting for goodwill, including amortization of goodwill. As the project was dropped from the FASB's agenda, any tentative decisions made will not become effective.

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Regulatory update

Sample letter to companies regarding disclosures pertaining to Russia's invasion of Ukraine and related supply chain issues

In May 2022, staff in the SEC's Division of Corporation Finance (Corp Fin) posted a sample letter in their article, "Companies Regarding Disclosures Pertaining to Russia's Invasion of Ukraine and Related Supply Chain Issues." They noted that companies may have disclosure obligations under the federal securities laws related to the direct or indirect impact that Russia's invasion of Ukraine and the international response have had or may have on their business. To satisfy these obligations, Corp Fin believes that companies should provide detailed disclosure, to the extent material or otherwise required, regarding:

1. *Direct or indirect exposure to Russia, Belarus, or Ukraine through their operations, employee base, investments in Russia, Belarus, or Ukraine, securities traded in Russia, sanctions against Russian or Belarusian individuals or entities, or legal or regulatory uncertainty associated with operating in or exiting Russia or Belarus.*
2. *Direct or indirect reliance on goods or services sourced in Russia or Ukraine or, in some cases, in countries supportive of Russia.*
3. *Actual or potential disruptions in the company's supply chain.*
4. *Business relationships, connections to, or assets in Russia, Belarus, or Ukraine.*

The financial statements may also need to reflect and disclose the impairment of assets, changes in inventory valuation, deferred tax asset valuation allowance, disposal or exiting of a business, deconsolidation, changes in exchange rates, and changes in contracts with customers or the ability to collect contract considerations. Corp Fin also notes that since Russia's invasion of Ukraine, many companies have experienced heightened cybersecurity risks, increased or ongoing supply chain challenges, and volatility related to the trading prices of commodities regardless of whether they have operations in Russia, Belarus, or Ukraine that warrant disclosure.

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In addition, Corp Fin states that, "Companies also should consider how these matters affect management's evaluation of disclosure controls and procedures, management's assessment of the effectiveness of internal control over financial reporting, and the role of the board of directors in risk oversight of any action or inaction related to Russia's invasion of Ukraine, including consideration of whether to continue or to halt operations or investments in Russia and/or Belarus."

We suggest that management and audit committees carefully review this sample letter as it relates to their exposure and business to ensure appropriate disclosures.

SEC proposals

ENHANCE AND STANDARDIZE CLIMATE-RELATED DISCLOSURES

In May 2022, the SEC extended the comment period for proposed rule changes that would require registrants to include **certain climate-related disclosures** in their registration statements and annual reports. The comment period for the release was originally scheduled to close on May 20, 2022. The new comment period ended on June 17, 2022. This proposal was discussed in the prior quarter's update.

ENHANCE DISCLOSURES BY CERTAIN INVESTMENT ADVISERS AND INVESTMENT COMPANIES ABOUT ENVIRONMENTAL, SOCIAL, AND GOVERNANCE (ESG) INVESTMENT PRACTICES

In May 2022, the SEC **proposed amendments** to rules and reporting forms to promote consistent, comparable, and reliable information for investors concerning funds' and advisers' incorporation of ESG factors. The proposed changes would apply to certain registered investment advisers, advisers exempt from registration, registered investment companies, and business development companies. The proposed amendments seek to categorize certain types of ESG strategies broadly and require funds and advisers to provide more specific disclosures in fund prospectuses, annual reports, and adviser brochures based on the ESG strategies they pursue. In order to complement the proposed ESG disclosures in fund prospectuses, annual reports, and adviser brochures, the proposal would require certain ESG reporting on Forms N-CEN and ADV Part 1A.

RULE CHANGES TO PREVENT MISLEADING OR DECEPTIVE FUND NAMES

In May 2022, the SEC **proposed amendments** under the Investment Company Act of 1940 that addresses certain broad categories of investment company names that are likely to mislead investors about an investment company's investments and risks. The proposed amendments are designed to increase investor protection by improving and clarifying the requirement for certain funds to adopt a policy to invest at least 80% of their assets in accordance with the investment focus that the fund's name suggests, updating the rule's notice requirements, and establishing recordkeeping requirements. The SEC is also proposing enhanced prospectus disclosure requirements for terminology used in fund names, and additional requirements for funds to report information on Form N-PORT regarding compliance with the proposed names-related regulatory requirements.

Digital assets and crypto investments

On May 16, 2022, at a FINRA conference, Chair Gensler made several speeches dealing with investor protections and specifically warned about investing in cryptocurrencies following the significant price declines. On May 17, 2022, in a speech at the 2022 NASAA Spring Meeting & Public Policy Symposium, Chair Gensler stated: "I think there's a need to bring greater investor protection to these crypto markets," and "The crypto-related events in recent weeks have highlighted yet again how important it is to protect investors in this highly speculative asset class."

Other developments

Accounting and reporting implications of the Russia/Ukraine war

As the impacts of Russia's invasion of Ukraine are being felt throughout the world, there will also be accounting and financial reporting implications that entities need to consider in addition to the humanitarian considerations.

The impacts from the war in Ukraine have already begun for many entities both directly and indirectly. Some of the areas where entities may be impacted include (not all-inclusive):

- *Asset impairment*
- *Equity method investments*
- *Discontinued operations*
- *Exit/disposal costs*
- *Consolidation*
- *Contingencies*

For each of the areas above, see "Accounting, financial reporting, and regulatory developments: First quarter 2022" for additional considerations on the financial reporting impacts. In addition to the items discussed above, entities should also consider other financial statement disclosures that may be appropriate. Entities that may be impacted should consider whether disclosure should be included in their risks and uncertainties disclosures or as a subsequent event.

If SEC registrants are considering including non-GAAP financial metrics in their filings as a result of the war in Ukraine, they should consider the SEC's rules and guidance on including non-GAAP metrics within their Form 10Q or Form 10K.

Standards adoption

Standards issued in 2022

Final ASU	Early adoption	Effective date
ASU 2022-03: *Fair value Measurement (Topic 820) — Fair Value Measurement of Equity Securities Subject to Contractual Sales Restrictions*	Yes	**Nonpublic:** *Fiscal years beginning after Dec. 15, 2024, and interim periods within those fiscal years.* **Public:** *Fiscal years beginning after Dec. 15, 2023, and interim periods within those fiscal years.*
ASU 2022-02: *Financial Instruments — Credit Losses (Topic 326) — Troubled Debt Restructurings and Vintage Disclosures*	Yes	**SEC registrants (excluding entities that qualify as SRCs):** Fiscal years beginning after Dec. 15, 2022, including interim periods within those fiscal years. **All other entities:** Upon adoption of ASU 2016-13
ASU 2022-01: *Derivatives and Hedging (Topic 815) — Fair Value Hedging — Portfolio Layer Method*	Yes	**Nonpublic:** *Fiscal years beginning after Dec. 15, 2023, and interim periods within those fiscal years.* **Public:** *Fiscal years beginning after Dec. 15, 2022, and interim periods within those fiscal years.*

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Standards issued in prior years effective 2022 or after

Final ASU	Early adoption	Effective date
ASU 2021-10: *Government Assistance (Topic 832) — Disclosures by Business Entities about Government Assistance*	Yes	Effective for all business entities for fiscal years beginning after Dec. 15, 2021.*,**
ASU 2021-09: *Leases (Topic 842) — Discount Rate for Lessees That Are Not Public Business Entities*	Yes — if early ASU 2016-02 is early adopted	**Nonpublic entities that have not adopted ASC 842:** *See ASU 2016-02** **Nonpublic entities that have adopted ASC 842:** *Fiscal years beginning after Dec. 15, 2021, and interim periods within fiscal years beginning after Dec. 15, 2022.** **Public business entities:** *Not eligible*
ASU 2021-08: *Business Combinations (Topic 805) — Accounting for Contract Assets and Contract Liabilities from Contracts with Customers*	Yes	**Nonpublic:** *Fiscal years beginning after Dec. 15, 2023, and interim periods within those fiscal years.* **Public:** *Fiscal years beginning after Dec. 15, 2022, and interim periods within those fiscal years.*
ASU 2021-07: *Compensation — Stock Compensation (Topic 718) — Determining the Current Price of an Underlying Share for Equity-Classified Share-Based Awards (a consensus of the Private Company Council)*	Yes	**Nonpublic:** *Fiscal years beginning after Dec. 15, 2021, and interim periods within fiscal years beginning after Dec. 15, 2022.** **Public business entities:** *Not eligible*
ASU 2021-05: *Leases (Topic 842) — Lessors — Certain Leases with Variable Payments*	Yes	**Nonpublic:** *Fiscal years beginning after Dec. 15, 2021, and interim periods within fiscal years beginning after Dec. 15, 2022.** **Public:** *Fiscal years beginning after Dec. 15, 2021, and interim periods within those fiscal years.***
ASU 2021-04: *Earnings Per Share (Topic 260), Debt — Modifications and Extinguishments (Subtopic 470-50), Compensation — Stock Compensation (Topic 718), and Derivatives and Hedging — Contracts in Entity's Own Equity (Subtopic 815-40): Issuer's Accounting for Certain Modifications or Exchanges of Freestanding Equity-Classified Written Call Options*	Yes	Effective for all entities for fiscal years beginning after Dec. 15, 2021.*,**
ASU 2021-01: *Reference Rate Reform (Topic 848): Scope*	Effective upon issuance	*Effective for the period March 12, 2020 through Dec. 31, 2022.*,***
Update 2020-11: *Financial Services — Insurance (Topic 944): Effective Date and Early Adoption*	Yes	**SEC registrants (excluding entities that qualify as SRCs):** *Fiscal years beginning after Dec. 15, 2022, including interim periods within those fiscal years.* **All other entities:** *Fiscal years beginning after Dec. 15, 2024, and interim periods beginning in fiscal years beginning after Dec. 15, 2025.*

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Update 2020-10: *Codification Improvements*	Yes	**See ASU**
Update 2020-08: *Codification Improvements to Subtopic 310-20, Receivables — Nonrefundable Fees and Costs*	Yes for nonpublic entities only — but no earlier than years beginning after Dec. 15, 2020	**Nonpublic:** *Fiscal years beginning after Dec. 15, 2021, and interim periods within annual periods beginning after Dec. 15, 2022.** **Public business entities:** *Fiscal years beginning after Dec. 15, 2020, and interim periods within these fiscal years.*
Update 2020-07: *Not-for-Profit Entities (Topic 958): Presentation and Disclosures by Not-for-Profit Entities for Contributed Nonfinancial Assets*	Yes	*Effective for annual periods beginning after June 15, 2021, and interim periods within annual periods beginning after June 15, 2022.*
Update 2020-06: *Debt — Debt with Conversion and Other Options (Subtopic 470-20) and Derivatives and Hedging — Contracts in Entity's Own Equity (Subtopic 815-40): Accounting for Convertible Instruments and Contracts in an Entity's Own Equity*	Yes — but no earlier than fiscal years beginning after Dec. 15, 2020	**SEC registrants (excluding entities eligible to be SRCs):** *Fiscal years beginning after Dec. 15, 2021, and interim periods within those fiscal years.*** **All other entities:** *Fiscal years beginning after Dec. 15, 2023, and interim periods within those fiscal years.*
Update 2020-05: *Revenue from Contracts with Customers (Topic 606) and Leases (Topic 842): Effective Date for Certain Entities*	Yes	REVENUE RECOGNITION **Nonpublic:** *Fiscal years beginning after Dec. 15, 2019, and interim periods within annual periods beginning after Dec. 15, 2020.* LEASES **Nonpublic:** *Fiscal years beginning after Dec. 15, 2021, and interim periods within annual periods beginning after Dec. 15, 2022.** **Public not-for-profit entities:** *Fiscal years beginning after Dec. 15, 2019 and interim periods within those fiscal years.*
Update 2020-04: *Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting*	Effective upon issuance	*Effective for the period March 12, 2020 through Dec. 31, 2022.*,***
Update 2020-03: *Codification Improvements to Financial Instruments*	Yes	*See ASU*
Update 2020-02: *Financial Instruments — Credit Losses (Topic 326) and Leases (Topic 842): Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 119 and Update to SEC Section on Effective Date Related to Accounting Standards Update No. 2016-02, Leases (Topic 842)*	Yes, if ASU 2016-13 adopted	*See ASU 2016-13* *See ASU 2016-02**
Update 2020-01: *Investments — Equity Securities (Topic 321), Investments — Equity Method and Joint Ventures (Topic 323), and Derivatives and Hedging (Topic 815): Clarifying the Interactions between Topic 321, Topic 323, and Topic 815*	Yes	**Nonpublic:** *Fiscal years beginning after Dec. 15, 2021, and interim periods within those fiscal years.** **Public business entities:** *Fiscal years beginning after Dec. 15, 2020, and interim periods within those fiscal years.***

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Update 2019-12: *Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes*	Yes	**Nonpublic:** *Fiscal years beginning after Dec. 15, 2021 and interim periods within annual periods beginning after Dec. 15, 2022.** **Public business entities:** *Fiscal years beginning after Dec. 15, 2020, and interim periods within these fiscal years.*
Update 2019-11: *Codification Improvements to Topic 326, Financial Instruments — Credit Losses*	Yes, if ASU 2016-13 adopted	*See ASU 2016-13*
Update 2019-10: *Financial Instruments — Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842): Effective Dates*	N/A	*See ASU 2016-02** *See ASU 2016-13* *See ASU 2017-12**
Update 2019-09: *Financial Services — Insurance (Topic 944): Effective Date*	N/A	*See ASU 2018-12*
Update 2019-05: *Financial Instruments — Credit Losses (Topic 326): Targeted Transition Relief*	Yes, if ASU 2016-13 adopted	*See ASU 2016-13*
Update 2019-04: *Codification Improvements to Topic 326, Financial Instruments — Credit Losses, Topic 815 Derivatives and Hedging, and Topic 825, Financial Instruments*	Yes	*See ASU*
Update 2019-01: *Leases (Topic 842): Codification Improvements*	Yes, if ASU 2016-02 adopted	*See ASU 2016-02**
Update 2018-20: *Leases (Topic 842): Narrow-Scope Improvements for Lessors*	Yes, if ASU 2016-02 adopted	*See ASU 2016-02**
Update 2018-19: *Codification Improvements to Topic 326, Financial Instruments — Credit Losses*	Yes, if ASU 2016-13 adopted	*See ASU 2016-13*
Update 2018-12: *Financial Services — Insurance (Topic 944): Targeted Improvements to the Accounting for Long-Duration Contracts*	Yes	**SEC registrants (excluding entities eligible to be SRCs):** *Fiscal years beginning after Dec. 15, 2022, and interim periods within those fiscal years.*** **All other entities:** *Fiscal years beginning after Dec. 15, 2024, and interim periods beginning after Dec. 15, 2025.*
Update 2018-11: *Leases (Topic 842): Targeted Improvements*	Yes, if ASU 2016-02 adopted	*See ASU 2016-02**
Update 2018-10: *Codification Improvements to Topic 842, Leases*	Yes, if ASU 2016-02 adopted	*See ASU 2016-02**

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Update 2018-01: *Leases (Topic 842) — Land Easement Practical Expedient for Transition to Topic 842*	Yes	*See ASU 2016-02**
Update 2017-04: *Intangibles — Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment*	Yes	**SEC registrants (excluding entities that qualify as SRCs):** *Fiscal years beginning after Dec. 15, 2019, including interim periods within those fiscal years.* **All other entities:** *Fiscal years beginning after Dec. 15, 2022, including interim periods within those fiscal years.*
Update 2016-13: *Financial Instruments — Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*	Yes, as of fiscal years beginning after Dec. 15, 2018, including interim periods within those fiscal years	**SEC registrants (excluding entities that qualify as SRCs):** *Fiscal years beginning after Dec. 15, 2019, including interim periods within those fiscal years.* **All other entities:** *Fiscal years beginning after Dec. 15, 2022, including interim periods within those fiscal years.*
Update 2016-02: *Leases (Topic 842)*	Yes	**Nonpublic:** *Fiscal years beginning after Dec. 15, 2021, and interim periods within annual periods beginning after Dec. 15, 2022.** **Public not-for-profit entities:** *Fiscal years beginning after Dec. 15, 2019 and interim periods within those fiscal years.* **Public business entities:** *Fiscal years beginning after Dec. 15, 2018, including interim periods within those fiscal years.*

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