QUARTERLY ACCOUNTING UPDATE WEBCAST – SPRING 2022

April 14, 2022

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Agenda

Topic
Financial reporting considerations related to current events
FASB standard-setting activity
Other accounting reminders and updates

Financial Reporting Considerations related to Current Events

Financial reporting considerations related to the Russia-Ukraine war and other macroeconomic factors

- SEC reporting
- Subsequent events
- Asset impairment
- Foreign currency matters
- Income taxes
- Cash
- Leases
- Fair value
- Risks and uncertainties
- Revenue contracts with customers
- Consolidation and equity method accounting
- Discontinued operations
- Exit or disposal costs
- Asset retirement obligations
- Employee termination benefits
- Going concern

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Monitoring inflation

Center for Audit Quality International Practices Task Force periodically accumulates and discusses certain inflation data

- Country economies are categorized based on their cumulative inflation rates considering the guidance in ASC 830, but does not include inflation data for all countries
- Helpful to a financial statement preparer in applying ASC 830, in conjunction with its internal controls over financial reporting, to reach a conclusion on whether a country's economy should be considered highly inflationary
- Discussion document typically published twice a year

Turkey – a highly inflationary economy

- Addendum to CAQ's *Document for Discussion Monitoring Inflation in Certain Countries* was issued March 16, 2022
- Recently released data shows that Turkey's three-year cumulative inflation exceeded 100% at the end of February 2022

FASB Standard-Setting Activity

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Selected ASUs effective in 2022 and other effective date reminders

ASU No.	Description	PBE*	Non-PBE*
2021-10	Disclosures by Business Entities about Government Assistance	X	X
2016-02	Leases (Topic 842)		X
2019-12	Simplifying the Accounting for Income Taxes		X
2020-01	Clarifying the Interactions between Topic 321, Topic 323, and Topic 815		X
2020-06	Accounting for Convertible Instruments and Contracts in an Entity's Own Equity	X	
2021-04	Issuer's Accounting for Certain Modifications or Exchanges of Freestanding Equity-Classified Written Call Options	X	

Effective date reminder
Refer to Annual Effective Date Reminder for full list of pronouncements that become effective on or after January 1, 2021

***Note:** Effective dates are for calendar year-end companies.

Recently issued FASB guidance, but not yet effective

ASU No.	Final ASU - title	PBE effective date*	Non-PBE effective date*
2022-01	Derivatives and Hedging (Topic 815): Fair Value Hedging—Portfolio Layer Method	2023	2024
2022-02	Financial Instruments—Credit Losses (Topic 326): Troubled Debt Restructurings and Vintage Disclosures.	2023	2023

***Effective dates are for calendar year-end companies**.

Evolution of guidance for hedging portfolio of financial assets

Better align hedge accounting and an entity's risk management activities

Pre-ASU 2017-12

- Very difficult to achieve hedge accounting for fair value hedges of interest rate risk of a portfolio of financial assets, particularly due to prepayment risk

ASU 2017-12

- Makes hedge accounting available for the "last-of-layer" of a closed portfolio of prepayable financial assets

ASU 2022-01

- Expands single-layer model in ASU 2017-12 to allow multiple-layer hedges of a single closed portfolio. Also, expands the layer to nonprepayable financial assets

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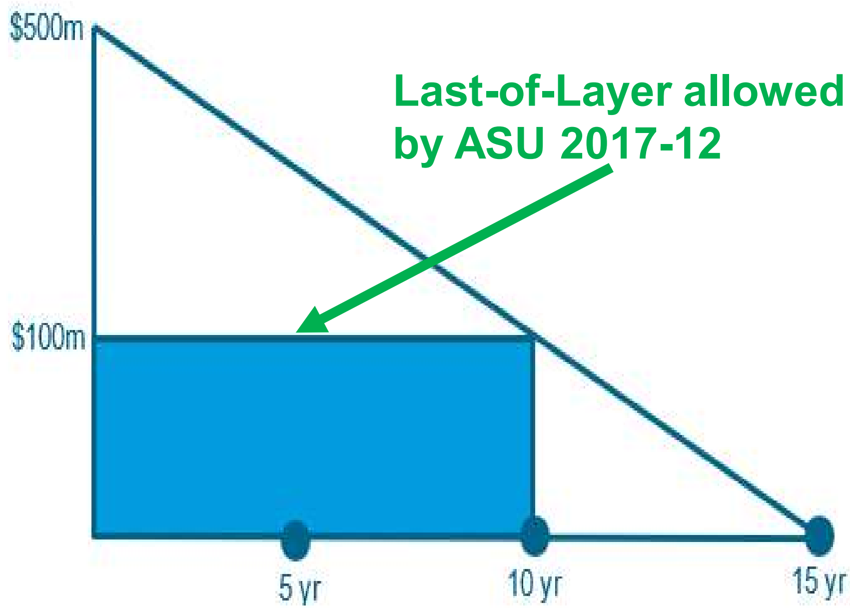
ASU 2022-01 – Portfolio layer method key provisions

- Permits fair value hedge accounting for a layer or layers of a closed portfolio
  - Portfolio may be comprised of prepayable and/or nonprepayable financial assets
  - Hedged risk is interest rate risk
  - Hedged item is a layer(s) of an amount(s)
- Provides flexibility to use different types of derivatives and layering techniques
- ASU provides guidance on the accounting for basis adjustments
- Entity must perform an analysis to support its expectation that the hedged layer will remain outstanding at the end of the hedge term
- Prepayment risk is not incorporated into the measurement of the hedged item

Last-of-Layer Method

Example

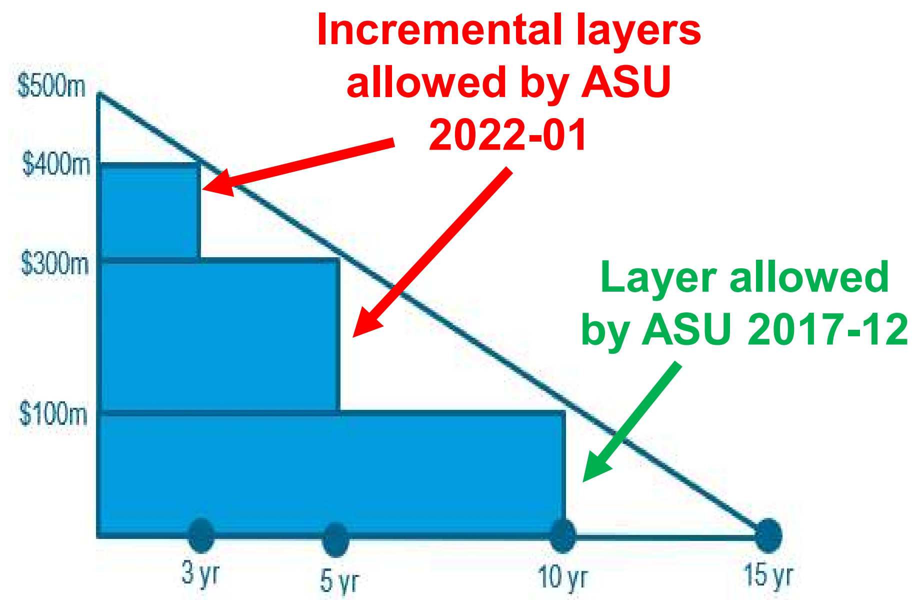
- $500 MM closed portfolio of fixed-rate prepayable loans
- After considering prepayments, defaults and other events, the following amounts are expected to be outstanding:
  - 3 Years → $400 million
  - 5 Years → $300 million
  - 10 Years → $100 million (last-of-layer)
- Last-of-layer is hedged with a $100 million 10-year interest rate swap



Portfolio Layer Method

Example

- Assume the same facts on the previous slide, except that the entity has adopted ASU 2022-01 and as a result, elects to hedge two layers in addition to the last-of-layer, for a total of three hedged layers
  - $100 million 3-yr layer hedged with a $100 million 3-yr interest rate swap
  - $200 million 5-yr layer hedged with a $200 million 5-yr interest rate swap
  - $100 million 10-yr layer hedged with a $100 million 10-yr interest rate swap



ASU 2022-01 - Effective date and transition

Entity	Effective for fiscal years…
PBEs	Beginning after December 15, 2022, and interim periods within those fiscal years
All other entities	Beginning after December 15, 2023, and interim periods within those fiscal years
Early adoption is permitted for any entity that has adopted ASU 2017-12 in the corresponding period	

Transition

- Upon adoption, multiple hedged layers of a single closed portfolio may be designated prospectively
- Amendments related to hedge basis adjustments, except for those related to disclosures, should be adopted on a modified retrospective basis
- Entities have a choice of adopting the amendments related to disclosures prospectively from the initial application date or retrospectively to each prior period presented after adopting ASU 2017-12
- If adopted in an interim period, the effect of adoption related to basis adjustments should be reflected as of the beginning of the fiscal year of adoption

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ASU 2022-01 - Key Takeaways

- Multiple layers of a closed portfolio of financial assets may be eligible for hedge accounting
- The closed portfolio may contain both prepayable and nonprepayable assets
- The reporting entity must perform an analysis (on an ongoing basis) to support its expectation that the aggregate of the hedged layers will remain outstanding during the hedge periods
- If a shortfall (breach) occurs or is anticipated and there are multiple hedged layers, an entity should determine which hedges to dedesignate or partially dedesignate in accordance with its accounting policy that specifies a systematic and rational approach to determining which hedge or hedges to dedesignate (or partially dedesignate)
    - Policy must be applied consistently

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Elimination of TDR recognition and measurement guidance

Instead of TDR model:

Determine whether a modified loan is a new or a continuation of the existing loan

- All receivable modifications evaluated under the loan refinancing and restructuring guidance in ASC 310-20-35-9 to 35-11

Determine an asset's contractual life over which to estimate credit losses

- Do not consider reasonably expected renewals, modifications, or extensions

Measure credit losses for modifications

- Discounted Cash Flow model would not be required

ASU 2022-02

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Additional disclosure requirements

Loan refinancings and restructurings	• New and enhanced disclosures for receivables for which there has been a modification to borrowers experiencing financial difficulties that have a change in contractual cash flows as a result of: • Principal forgiveness • Interest rate reductions • Other-than-insignificant payment delays • Term extensions
Vintage Disclosures—Gross Writeoffs	• PBEs must disclose current-period gross writeoffs by year of origination for financing receivables and net investments in leases

ASU 2022-02

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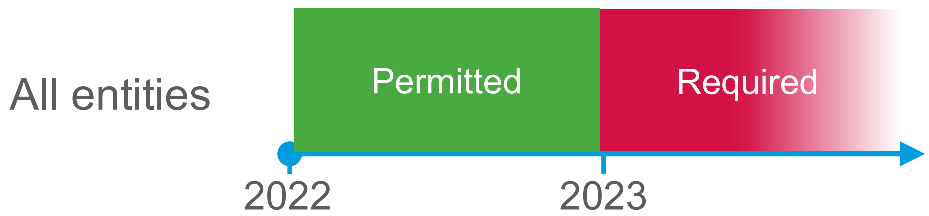
Effective date

Effective date for calendar year-ends



Transition

- Prospective, except for possible election to apply modified retrospective transition method for the recognition and measurement of TDR

ASU 2022-02

FASB Standard-Setting Activity

FASB Technical Agenda

Status of select projects on FASB's technical agenda

Topic	Status
Identifiable intangible assets and subsequent accounting for goodwill	Initial deliberations
Consolidation reorganization and targeted improvements	Redeliberation
Distinguishing liabilities from equity phase 2	Initial deliberations
Accounting for investments in tax credit structures using the proportional amortization method	Initial deliberations
Fair value measurement of equity securities subject to contractual sale restrictions	Redeliberation
Credit losses – Acquired financial assets	Initial deliberations
Improving the accounting for asset acquisitions and business combinations	Initial deliberations
Joint venture formations	Initial deliberations
Lease modifications	Redeliberation
Reference rate reform – Fair value hedging	Initial deliberations

Other Accounting Reminders and Updates

Interim Tax Reporting - Estimated annual effective tax rate (EAETR) reminders

Step 1
Estimate AETR
(ASC 740-270-25-2)

Step 2
Record tax on current year-to-date basis
(ASC 740-270-30-5)

Step 3
Recognize discrete items
(ASC 740-270-25-2)

Step 4
Prepare required disclosures
(ASC 740-270-50-1)

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Digital assets and use of distributed ledger technology

- Increased acceptance of digital assets in exchange for goods and services has resulted in “traditional” businesses holding digital assets for the first time
- More interest in using digital assets within an entity’s investment strategy has also resulted in businesses holding digital assets for the first time

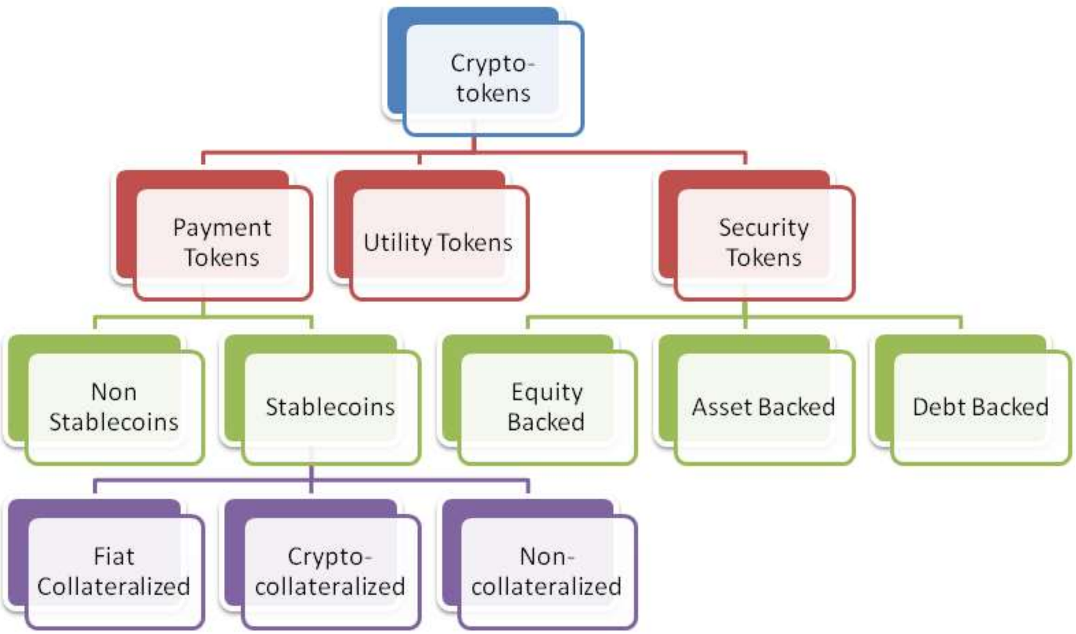
RAPID DEVELOPMENT OF NEW USE CASES, PRODUCTS, SERVICES WITHIN DIGITAL ASSET ECOSYSTEM

NEW USE CASES FOR DISTRIBUTED LEDGER TECHNOLOGY (DTL) FROM “TRADITIONAL” BUSINESSES, FOR EXAMPLE USING NFTS FOR MEMBERSHIPS

Matters to consider when purchasing digital assets or receiving digital assets as payment for goods or services

- Accounting and financial reporting considerations
- Custody/storage
  - Self custody
  - Third-party custodian
  - Hot wallets, cold wallets, wallet controls
- Governance
- Internal policies and controls
- Valuation
- Income tax
- Other

General categories of digital asset tokens



* Stablecoins can also be viewed as Asset Tokens

Utility Tokens

- Exchanged or received for products, services, or content (distributed computing/storage)

Security Tokens*

- Digital representations of assets (gold, oil, real estate, IP, art)
- Digital representations of traditional securities (equities, bonds, derivatives, futures, etc.) – “Security tokens”

Payment Tokens (Cryptocurrencies)

- Intended to be used as a currency or store of value, for example:
  - Bitcoin, Ripple (XRP)
  - Stablecoins (USDC)*

Hybrid Tokens

- Share characteristics of multiple categories above

Cryptocurrency classification and measurement considerations

- How should an entity (that does not apply investment company or other specialized-industry guidance) account for purchases of cryptocurrencies for cash?

  Cryptocurrencies are the type of digital assets that:

  a. Function as a medium of exchange and
  b. Have all the following characteristics (not all-inclusive):
     i. Not issued by a jurisdictional authority, e.g., a sovereign government
     ii. Do not give rise to a contract between the holder and another party
     iii. Not considered a security

  − Examples of cryptocurrencies include Bitcoin, Bitcoin Cash and Ether

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Cryptocurrencies are not…

- Cryptocurrencies are <u>not</u> cash or cash equivalents when they are not considered legal tender and are not backed by sovereign governments. In addition, these cryptocurrencies typically do not have a maturity date and have traditionally experienced significant price volatility
- Cryptocurrencies are <u>not</u> financial instruments or financial assets if they are not cash or an ownership interest in an entity and if they do not represent a contractual right to receive cash or another financial instrument
  - Stablecoins are a category of cryptocurrencies that may meet the definition of a financial instrument
- Cryptocurrencies do <u>not</u> meet the definition of inventory or property, plant and equipment because they are not tangible

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Cryptocurrencies are…

- Cryptocurrencies are commonly viewed as intangibles, excluding stablecoins that meet the definition of a financial instrument
  - If there is no inherent limit imposed on the useful life of the cryptocurrency to the entity, then the cryptocurrency would be classified as an indefinite-lived intangible asset
  - As intangible assets, cryptocurrencies purchased for cash would initially be measured at cost, and then subject to impairment testing.

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Classification and measurement considerations for other digital assets

- Cryptocurrencies represent a subset of the digital assets currently available and held by entities. Other categories of digital assets include:
  - Utility tokens
  - Asset tokens (including security tokens)
  - Hybrid tokens
  - Non-fungible tokens (NFTs)
- In practice, the hierarchy of applicable guidance used to consider the appropriate accounting for these assets is similar to that used for cryptocurrencies. If these tokens do not meet the definitions of cash, cash equivalents, financial instruments/assets, inventory, property, plant and equipment or intangibles, then an entity should consider if they represent a prepayment for goods or services, or provide an interest in an underlying asset or issuing entity

Other considerations when classifying or measuring other digital assets

- Consider the digital asset's terms and characteristics
  - Is the digital asset a financial instrument/asset, a commodity or an intangible?
- Consider the business purpose for holding the digital asset
  - Entities may hold different digital assets for different business purposes or hold different stores or buckets of the same digital asset for different purposes
    - For example, an entity might hold a digital asset in cold storage for value appreciation and hold another store of the same digital asset for active trading

Receiving digital assets in exchange for goods and services

- When an entity contracts with a customer and agrees to accept a digital asset as consideration for a good or service, need to determine the appropriate application of ASC 606
- Receipt of the digital asset would generally be regarded as noncash consideration under ASC 606
- Noncash consideration is measured at contract inception when determining the transaction price for the revenue contract under ASC 606
- When a transaction allows for the receipt of digital assets in the future, entities need to consider ASC 815 to determine whether this potentially represents a derivative or a hybrid instrument

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Interpretive guidance and standard-setting activity

- AICPA Practice Aid – Accounting for and auditing of digital assets
- SEC Staff Accounting Bulletin No.121
- FASB technical agenda

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Save the date!
Next quarterly
accounting update

QUESTIONS AND CLOSING REMARKS

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THANK YOU FOR YOUR TIME AND ATTENTION

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