



Real estate accounting and reporting

**The impact of new standards
and guidance**

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As a leader in real estate financial reporting, KPMG LLP (KPMG) creates this report annually to assist real estate companies with their financial accounting, regulatory, and compliance reporting requirements.

This year's report provides technical guidance on current requirements, including the new revenue standard that is now in effect for public companies, as well as looks ahead to highlight accounting rules that take effect in 2019, such as the new leasing requirements and other upcoming changes to existing U.S. GAAP requirements. Additionally, we offer some brief insights on the current regulatory environment facing our industry.

With the recent tax regulatory changes and continuing disruption in the real estate sector, applying evolving accounting rules to your business remains a clear and serious challenge. This document is intended to provide our perspectives on how to address the key issues you will face; we would be happy to discuss your specific situations or objectives in more detail.

We look forward to continuing to work with you to effectively navigate this increasingly dynamic accounting and regulatory environment, as well as support your efforts to achieve your broader business objectives.

Thank you.



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Accounting reminders - Effective in 2018 for public companies and 2019 for nonpublic companies

Reminders for certain new guidance effective January 1, 2018, for public calendar year-end companies and effective January 1, 2019, for nonpublic calendar year-end companies.

Equity investments and financial liabilities

The FASB issued a new accounting standard¹ that significantly changes the income statement effect of equity investments held by an entity and the recognition of changes in fair value of financial liabilities when the fair value option is elected.

Under the new standard, entities must measure equity investments with readily determinable fair values at fair value and recognize changes in fair value in net income. For equity investments without readily determinable fair values, entities have the option to either measure these investments at fair value, or at cost adjusted for changes in observable prices minus impairment. Changes in measurement under either alternative must be recognized in net income. Because entities must recognize changes in the measurement of equity investments in net income, income statement volatility will increase.

Entities that elect the fair value option for financial liabilities must recognize changes in fair value attributable to instrument-specific credit risk in other comprehensive income (OCI) so that changes in an entity's credit risk will not affect earnings when the fair value option is elected.

The new standard is effective for public business entities for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. For all other entities, it is effective for fiscal years beginning after December 15, 2018, and interim periods in fiscal years beginning after December 15, 2019.

Early adoption of the standard is permitted for nonpublic business entities for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years.

Statement of cash flows: presentation and classification issues

Restricted cash presentation

In November 2016, the FASB issued new guidance² requiring that the statement of cash flows explain the

change in the total of cash and cash equivalents, including amounts generally described as restricted cash and restricted cash equivalents.

When these total amounts as of the beginning or end of any period presented are included in more than one line item within the statements of financial position, companies should disclose the amounts and line items in which cash and cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents, are reported in each statement of financial position presented. The new guidance also requires an entity to disclose the nature of restrictions on cash and cash equivalents.



¹ FASB Accounting Standards Update No. 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities, and FASB Accounting Standards Update No. 2018-04, Investments—Debt Securities (Topic 320) and Regulated Operations (Topic 980)

² FASB Accounting Standards Update No. 2016-18, *Restricted Cash*

The new guidance became effective for public business entities in interim and annual periods beginning after December 15, 2017. For all other entities, it is effective for annual periods beginning after December 15, 2018, and interim periods within fiscal years beginning after December 15, 2019. The new guidance requires retrospective application. Early adoption is permitted and transition disclosures are required in the first interim and annual period of adoption.

Classification of certain cash receipts and cash payments

The FASB issued new guidance³ addressing eight cash flow issues that are expected to reduce diversity in practice and improve financial reporting. Those issues most relevant to the real estate industry include:

Debt prepayment or extinguishment costs. The new guidance states that cash payments for debt prepayment or extinguishment costs should be classified as cash outflows for financing activities.

Settlement of zero-coupon bonds. The new guidance states that the portion of the cash payment at settlement attributable to the accreted interest should be classified as a cash outflow for operating activities. The portion of the cash payment attributable to the principal (i.e., original proceeds received) should be classified as a cash outflow for financing activities. At settlement, entities should classify the entire cash payment associated with other bonds issued at a discount as a cash outflow for financing activities.

Contingent consideration payments made after a business combination. The new guidance states that cash payments made after a business combination for the settlement of a contingent consideration liability should be separated and classified as:

- A cash outflow for financing activities for the portion of the total cash payment not to exceed the amount of the contingent consideration liability recognized as the acquisition-date fair value (including measurement period adjustments). This classification presumes the amount is not paid at the time of purchase or soon before or after the business combination occurred. Otherwise it would be classified as a cash outflow for investing activities.

- A cash outflow for operating activities for the amount paid in excess of the amount of the contingent consideration liability recognized as the acquisition-date fair value (including measurement period adjustments).

Distributions received from equity method investees.

The new guidance requires an accounting policy election to use either the cumulative-earnings approach or the look-through approach for all investees.

Under the cumulative-earnings approach, all distributions received from the investee are presumed to be returns on investment and classified as operating inflows. However, if the investor's cumulative distributions, excluding distributions in prior years that were determined to be returns of investment, exceed the investor's cumulative equity in earnings, the current period distribution up to this excess is considered a return of investment and classified as investing inflows.

Under the look-through approach, distributions received are classified based on the specific facts and circumstances. If the entity does not have the information necessary to evaluate the specific facts and circumstances of a distribution received from an investee, it applies the cumulative-earnings approach to determine the classification.

For public business entities, the guidance became effective for annual periods beginning after December 15, 2017, and for interim periods beginning after December 15, 2017. For all other entities, the guidance is effective for annual periods beginning after December 15, 2018, and for interim periods beginning after December 15, 2019. Full retrospective transition is required, with a provision for impracticability. Early adoption is permitted; however, an entity must adopt all issues at the same time.

Clarifying the definition of a business

In January 2017, the FASB issued guidance⁴ that provides a new framework for determining whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. The guidance states that an integrated set of activities and assets (a set) is a business if it has, at a minimum, an input and a substantive process that together contribute to the ability to create outputs. The guidance creates an initial screening test that reduces the population of a potential businesses before an entity analyzes whether there is an input and a substantive process in the set.

³ FASB Accounting Standards Update No. 2016-15, *Classification of Certain Cash Receipts and Cash Payments*

⁴ FASB Accounting Standards Update No. 2017-01, *Clarifying the Definition of a Business*

The following is an overview of the two-step test:

step 1

Is substantially all of the fair value of the gross assets acquired concentrated in a single (group of similar) identifiable asset(s)?

If yes, the set is not a business. If no...

step 2

Evaluate whether an input and a substantive process exist...

Does the set have outputs?

If yes...

The set is a business if it includes an input or inputs and:

- Organized workforce with skills, knowledge, or experience critical to continue producing outputs;
- Process that cannot be replaced without significant cost, effort, or delay; **or**
- Process that is considered unique or scarce.

If no...

The set is a business if it includes:

- Employees that form an organized workforce with skills, knowledge, or experience to perform an acquired process (or group of processes) that is critical to the ability to create outputs; **and**
- Input(s) that the workforce could develop or convert into outputs.

Fewer real estate transactions will qualify as business acquisitions under the new guidance than qualify today, but it may be difficult to determine whether assets are combined or considered similar in applying the screening test. See next column for a real estate example that illustrates the definition.

Example

Facts

- REIT acquires 10 single-family homes in the Washington, DC metro area. The acquisition includes the land, building, property improvements, and in-place leases.
- Each single-family home has a different layout (e.g., floor plan, square footage, and design). The lessees are a similar class of customers.
- No workforce or other assets are acquired in the transaction.

Analysis

Step 1: REIT identifies the individual assets in the set and concludes that the land, building, property improvements, and in-place leases at each property are considered a single asset for purposes of Step 1. The building and property improvements are attached to and cannot be physically removed and used separately from the land without incurring significant costs or reducing their fair value. The in-place lease intangibles for each home are required to be combined with the leased asset for the screening test.

REIT concludes that the 10 homes are a group of similar assets based on the nature of the homes (single-family) and similar risks associated with managing this portfolio of homes. That is, the risks of operating the homes and managing the tenants are not significantly different.

Because there are no other assets in the set, REIT concludes that the fair value of the gross assets acquired is concentrated in a group of similar identifiable assets (the 10 homes) and Step 1 is met.

Step 2 is not necessary.

Conclusion

The acquired set meets the initial screening test (Step 1). Therefore, the acquired set is not a business.

The new guidance became effective for public business entities for annual and interim periods in fiscal years beginning after December 15, 2017. For all other entities, it is effective for annual periods in fiscal years beginning after December 15, 2018, and interim periods in fiscal years beginning after December 15, 2019. Entities may early adopt the new guidance and apply it to transactions that have not been reported in financial statements that have been issued or made available for issuance. No transition disclosures are required.

Clarifying the scope of derecognition of nonfinancial assets

In February 2017, the FASB issued new guidance⁵ that clarifies that the guidance in ASC Topic 610–20 on accounting for derecognition of a nonfinancial asset and an in-substance nonfinancial asset applies only when the asset (or asset group) does not meet the definition of a business and is not a not-for-profit entity. An in-substance nonfinancial asset is defined as one that is included in a contract or consolidated subsidiary in which substantially all of the fair value (excluding cash and cash equivalents) is concentrated in nonfinancial assets.

The new guidance applies to transfers and nonmonetary exchanges of interests in a subsidiary that contains only nonfinancial assets and in-substance nonfinancial assets when the seller retains a noncontrolling equity interest. The seller will account for the noncontrolling interest as noncash consideration and measure it at fair value. The guidance eliminates the partial profit recognition models in real estate and nonmonetary transactions guidance when a seller retains a noncontrolling interest in the transferred asset. A seller will recognize its full gain in earnings when it loses its controlling financial interest and would not recognize a gain in earnings when it retains a controlling financial interest.

Because Subtopic 610–20 applies when real estate (or in-substance real estate) does not meet the definition of a business based on the new guidance that clarifies the definition of a business, we believe most noncustomer real estate sales fall within its scope. Additionally, sales of noncontrolling ownership interests accounted for under the equity method that are considered in-substance real estate under current U.S. GAAP will now

be accounted for under transfer and servicing guidance (ASC 860) regardless of whether the buyer is a customer or noncustomer.

The guidance became effective for public business entities for annual and interim periods in fiscal years beginning after December 15, 2017. For all other entities, it is effective for annual periods beginning after December 15, 2018, and for interim periods beginning after December 15, 2019.

The new guidance was effective at the same time as the new revenue recognition standard. At adoption, an entity applies the new definition of a business to determine which transactions are in the scope of the new guidance, regardless of the entity's transition method.

Revenue recognition standard now effective for public companies

At long last, the mandatory adoption date for the revenue recognition standard⁶ is here. Calendar year-end public companies were required to adopt and apply the requirements of the standard in the first quarter of 2018. Initial transition disclosures about the adoption of the revenue adoption standard have been informative about trends in adopt methods and other disclosure matters.

Adoption method insights

Company filings show that the majority of adopters are transitioning using the cumulative-effect method. An entity adopting the standard using the cumulative-effect method does not revise its historical financial statements. However, to inform investors about the effects of adoption, the cumulative-effect adopter will, in effect, need to maintain dual-reporting to comply with the transition disclosure requirements in the year of adoption. Those companies will need to implement new (or redesign existing) processes and controls to track two accounting methods during the year of adoption to disclose:

- The amount by which applying ASC 606 affects each financial statement line item in the current period
- The amount and reason for the significant changes between the reported results under ASC 606 and those that would have been reported under legacy US GAAP (ASC 605, Revenue Recognition).

⁵ FASB Accounting Standards Update No. 2017-05, *Clarifying the Scope of Asset Derecognition Guidance and Accounting for Partial Sales of Nonfinancial Assets*

⁶ ASC Topic 606, *Revenue from Contracts with Customers*

Management's discussion and analysis (MD&A) disclosures

In addition to the required transition disclosures, many companies are providing additional information in MD&A about the effect of the adoption on prior periods. This presentation is considered a supplemental presentation—not non-GAAP or pro forma financial information. A registrant is permitted to include comparable prior periods under ASC 606 to facilitate comparability of MD&A disclosures as long as it follows certain guidance in the supplemental presentation:

- The discussion is not more prominent than the historical MD&A discussion.
- The discussion is limited to only those items for which the registrant can determine the effects (e.g. a registrant should not present a supplemental measure of gross profit or operating income unless the affected costs can be appropriately adjusted).
- The income statement line items presented are limited to those that would have been affected—a registrant should not present a full income statement.
- The registrant's discussion may address net income for the prior periods if the registrant is able to determine the effects on all affected income statement line items.

Alternatively, a registrant may present the 2018 results determined under legacy U.S. GAAP similar to what is required by AC 606 in the notes to the financial statements. This option would be permitted in 2018 only, the year of adoption, and the registrant would need to:

- Provide disclosures comparable to those required in the notes to the financial statements under ASC 250, *Accounting Changes and Error Corrections*

- Display the ASC 606 results prominently
- Limit the discussion about the ASC 605 amounts to comments that enhance an investor's understanding of comparability.

Regardless of whether the registrant chooses this option, it should disclose assumptions or practical expedients used.

Control changes with implementation

Companies that have materially changed their internal controls over financial reporting (ICFR) are required to disclose the changes in their interim and annual filings. Though not required, a number of companies have disclosed the effect of adoption on processes and controls even when management did not believe those changes were material.

When considering whether to disclose internal control changes, it may be helpful to think about the controls associated with adoption in two groups: "one-time" controls put in place to adopt and transition to the new standard, and "ongoing" controls needed to account for current and future transactions under ASC 606.

Effective dates for private companies forthcoming

The effective date for the new standard is approaching for private companies, with the guidance being effective for annual periods in fiscal years beginning after December 15, 2018, and interim periods in fiscal years beginning after December 15, 2019.



2 Accounting reminders— Effective in 2018 for nonpublic companies

Reminders for certain new guidance effective January 1, 2018, for nonpublic calendar year-end companies.

Accounting for share-based payments simplified

In March 2016, the FASB issued new guidance⁷ intended to improve the accounting for share-based payment transactions. Under the new guidance:

- Excess tax benefits or deficiencies related to share-based payments are recognized through the income statement instead of equity and are treated as discrete items (i.e., are excluded when computing the estimated annual effective tax rate).
- Excess tax benefits are classified as an operating activity in the statement of cash flows.
- Entities may elect an accounting policy to either estimate the number of forfeitures (current U.S. GAAP) or account for forfeitures when they occur.
- Entities can withhold up to the maximum individual statutory tax rate without classifying the awards as a liability. The cash paid to satisfy the statutory income tax withholding obligation is classified as a financing activity in the statement of cash flows.
- Nonpublic entities are allowed to use a practical expedient to determine the expected term of certain share-based awards.

The new guidance became effective for all nonpublic entities for fiscal years beginning after December 15, 2017 and interim periods within those years beginning after December 15, 2018. Early adoption is permitted in any interim or annual period provided that the entire ASU is adopted.

⁷ FASB Accounting Standards Update No. 2016-09, Improvements to Employee Share-Based Payment Accounting





Looking ahead to new standards and guidance

Preparing for ASC 842, Leases

The leases standard takes effect for public companies in 2019 and companies are beginning to identify more detailed implementation issues. Public companies have raised questions about the accounting for real estate sale-leaseback transactions that take place before they adopt the leases standard but after they adopt the new revenue standard and about how to apply the optional short-term lease exemption. They also have questions about whether it is appropriate to use a recognition threshold below which they would not recognize lease assets and liabilities.

Real estate sale-leasebacks and interaction with the revenue recognition standard

In a sale-leaseback transaction, one entity (the seller-lessee) transfers an asset to another entity (the buyer-lessor) and subsequently leases that asset back from the buyer-lessor. Pivotal to determining the accounting for that transaction is whether a sale (for the seller-lessee) and purchase (for the buyer-lessor) has taken place.

Companies have raised questions about which guidance a seller-lessee should use when evaluating whether a transfer of real estate qualifies as a sale in a sale-leaseback after they adopt the revenue recognition standard, but before adopting the leases standard. These questions have arisen in part because the revenue recognition standard supersedes the real estate-specific revenue guidance in ASC 360–20. Additionally, after the effective date of the leases standard, sale-leaseback transactions will result in a sale/purchase of the transferred asset only if the sale requirements in the revenue recognition standard and two additional requirements specific to the sale-leaseback guidance in the new leases standard are met.

In response to those questions, we note that it is important to keep in mind certain facts:

- None of the ASUs related to adopting the revenue recognition standard amended the sale-leaseback guidance in ASC 840–40. Therefore, adopting the revenue recognition standard does not change an entity’s sale-leaseback accounting unless it adopts the leases standard concurrently.
- ASC 360–20 is superseded for only those sale-leaseback transactions that take place after the effective date of the leases standard.
- There is no concept of a failed purchase for the buyer-lessor in a sale-leaseback transaction under ASC 840–40. A failed purchase can only occur once an entity has adopted the leases standard.

Using recognition thresholds under the leases standard

The FASB observed that in addition to accounting for some leases at a portfolio level, companies would likely be able to reduce their costs of applying the leases standard by adopting reasonable thresholds below which they would not recognize lease assets and lease liabilities. The FASB stated that an entity may adopt a practice of using a recognition threshold under the leases standard consistent with its accounting policies to use thresholds in other areas of U.S. GAAP, such as when determining whether to capitalize purchases of property, plant, and equipment (PP&E). A lessee should separately evaluate the effects of not recognizing the lease liability and the ROU asset on the balance sheet (both individually and in the aggregate) when establishing a capitalization threshold for leases. And, if the lessee also intends to exclude leases below the threshold from its lease disclosures, the threshold should consider the effect on the completeness and accuracy of those disclosures.

Improvements to the lease guidance

In July 2018, the FASB issued targeted improvements⁸ creating an additional transition method, and a lessor practical expedient to not separate lease and nonlease components if specific criteria are met.

Optional transitional relief. The new transition method allows companies to use the effective date of the leases standard as the date of initial application on transition. Companies that elect this transition option will not adjust their comparative period financial information for the effects of ASC 842, not make the new required lease disclosures for periods before the effective date, and carry forward their ASC 840 disclosure for comparative periods.

⁸ FASB Accounting Standards Update No. 2018-11, Leases (Topic 842): *Targeted Improvements*

Lessor separation of lease and nonlease components.

The practical expedient permits lessors to make an accounting policy election by class of underlying asset to not separate lease and nonlease components if two specific criteria are met. The first criteria is the timing and pattern of transfer to the lessee of the lease component and the nonlease component(s) associated with that lease component are the same. The second is that the lease component, if accounted for separately, would be classified as an operating lease.

If the practical expedient has been elected and a contract includes multiple nonlease components—one or more that meet(s) the timing and pattern of transfer criterion and one or more that does (do) not—the lessor combines the nonlease component(s) that meets the first criterion with the lease component and separates nonlease components that do not.

If the nonlease component(s) is (are) the predominant component(s) of the combined component—i.e., because the lessee would reasonably be expected to ascribe more value to the nonlease component(s)—the lessor should account for the combined component under ASC 606, as a single ASC 606 performance obligation, rather than under the leases guidance in ASC 842.

In those cases, the lessor:

- Uses the same measure of progress for the combined ASC 606 component as it used when determining eligibility for combination of the lease and non lease component(s) (generally time-elapsed)
- Accounts for all variable payments related to any good or service, including the lease, that is part of the combined ASC 606 performance obligation under the guidance on variable consideration in ASC 606.

All other combined components are accounted for under ASC 842 as a single lease component. This includes situations in which the lease component and nonlease component(s) are equally significant to the contract. If the combined component is accounted for under ASC 842

as a single lease component, the lease is classified as an operating lease by default; no lease classification test is performed. In these cases, all variable payments under the contract are accounted for as variable lease payments under ASC 842.

Proposed narrow-scope improvements for lessors

The FASB's proposed amendments⁹ would:

- Add a practical expedient permitting lessors to present collections of sales and other similar taxes that arise from a specific lease transaction net of the lessor's payment of such taxes
- Require a lessor to present lessor costs and payments made by the lessee directly to a third party (e.g., an insurer) on a net basis when the lessor cannot readily determine the amounts paid by the lessee to the third party. Lessor costs include property taxes on the underlying asset for which the lessor is the primary obligor, and insurance on the underlying asset required by the lease contract for which the lessor is the primary beneficiary. This proposal might apply to lessor costs of insurance on the underlying asset when the lessee is the policy owner and is not required, nor expected, to report its premiums to the lessor, or insures the asset through an umbrella policy.

The proposed amendments would also clarify that:

- A lessor should allocate variable payments between the lease and non-lease components of a lease contract under the allocation guidance in ASC 606
- A lessor should allocate variable payments between the lease and nonlease components of a lease contract under the allocation guidance in ASC 606.

The leasing standard will be effective for public companies for annual and interim periods in fiscal years beginning after December 15, 2018. For private companies, the standard will be effective for annual periods in fiscal years beginning after December 15, 2019, and interim periods in fiscal years beginning after December 15, 2020.

⁹ Proposed Accounting Standards Update—Leases (Topic 842): *Narrow-Scope Improvements for Lessors*

Simplifying goodwill impairment accounting

Current Requirements	New Guidance
Indicators of impairment at an interim date require a quantitative test for goodwill impairment	No change
Optional Step 0 allows qualitative assessment of whether it is more likely than not that goodwill is impaired (annual test only)	No change
Step 1 of the goodwill impairment test identified potential impairment	Single-step test identifies and measures impairment
Step 2 of the goodwill impairment test measures the impairment	Eliminated
Qualitative assessment identifies impairment for reporting units with zero or negative carrying amounts. When impairment is identified, perform Step 2 to measure the impairment.	Replaced. Entities must disclose the amount of goodwill allocated to each reporting unit with zero or negative carrying amounts and the related reportable segment.

In January 2017, the FASB issued new guidance¹⁰ to simplify the subsequent measurement of goodwill by removing the second step of the goodwill impairment test. An entity would perform its annual or interim goodwill impairment test by comparing the fair value of a reporting unit to its carrying amount. If the reporting unit's carrying amount exceeds its fair value, the difference, up to the carrying amount of the goodwill allocated to the reporting unit, would be recognized as an impairment in goodwill.

The new guidance is effective for annual and interim periods in fiscal years beginning after December 15, 2019 for public business entities that file with the SEC and for annual and interim periods in fiscal years beginning after December 15, 2020 for public business entities that do not file with the SEC. For entities that are not public business entities, the new guidance will be effective for annual and interim periods in fiscal years beginning after December 15, 2021. Early adoption is permitted for goodwill impairment tests with measurement dates after January 1, 2017.

Changes to hedge accounting

In August 2017, the FASB issued new guidance¹¹ that changes the recognition and presentation requirements of hedge accounting including eliminating the requirement to separately measure and report hedge ineffectiveness and adding a requirement to present all the income statements effects of hedge accounting in the same caption as the hedged item.

The guidance also provides new alternatives for applying hedge accounting to additional hedging strategies, measuring the hedged item in fair value hedges of interest rate risk, reducing the cost and complexity of applying hedge accounting by easing the requirements for effectiveness testing, hedge documentation and application of the critical terms match method, and reducing the risk of material error corrections if an entity applies the shortcut method inappropriately.

The new guidance is effective for public business entities for annual and interim periods in fiscal years beginning after December 15, 2018. For other entities, it is effective for annual periods in fiscal years beginning after December 15, 2019 and interim periods in fiscal years beginning after December 15, 2020. Early adoption is permitted at any time. If adopted at a period other than the beginning of a fiscal year, cumulative effect adjustments are reflected as of the beginning of the fiscal year.

¹⁰ FASB Accounting Standards Update No. 2017-04, *Simplifying the Test for Goodwill Impairment Improvements*

¹¹ FASB Accounting Standards Update No. 2017-12, *Targeted Improvements to Accounting for Hedging Activities*

Improvements to nonemployee share-based payment accounting

In June 2018, the FASB issued guidance¹² eliminating the separate accounting model for nonemployee share-based payment awards and generally requiring companies to account for share-based payment transactions with nonemployees in the same way as share-based payment transactions with employees.

The accounting remains different for attribution and a contractual term election for valuing nonemployee equity share options. Attribution, which represents how the equity-based payment cost is recognized over the vesting period, will continue to be applied for nonemployee awards as if the company issuing equity had paid cash for the goods and/or services. Accordingly, an entity should consider the nature of what it received to determine the appropriate period and pattern in which to recognize the cost.

The new guidance is effective for public business entities for annual and interim periods in fiscal years beginning after December 15, 2018. For other entities, it is effective for annual periods in fiscal years beginning after December 15, 2019 and interim periods in fiscal years beginning after December 15, 2020. Early adoption is allowed, but no earlier than the entity's adoption date of ASC 606.

Changes to fair value measurement disclosures

As part of its disclosure framework project, the FASB issued guidance¹³ in August 2018 that eliminates, amends, and adds disclosure requirements for fair value measurements. The amended fair value disclosures are part of the FASB's disclosure review project that tests the effectiveness of its disclosure framework. These amendments are expected to reduce costs for preparers while providing more decision-useful information for financial statement users.



¹² FASB Accounting Standards Update No. 2018-07, *Improvements to Nonemployee Share-Based Payment Accounting*

¹³ FASB Accounting Standards Update No. 2018-13, *Changes to the Disclosure Requirements for Fair Value Measurement*

The FASB eliminated four disclosures:	The FASB amended and clarified four disclosures:	The FASB also added two new disclosure requirements for public companies:
<ul style="list-style-type: none"> — Amount of, and reasons for, transfers between Level 1 and Level 2 of the fair value hierarchy — The policy of timing of transfers between levels of the fair value hierarchy — The valuation processes for Level 3 fair value measurements — For nonpublic companies, the changes in unrealized gains and losses for the period included in earnings for recurring Level 3 fair value measurements for instruments held at the end of the reporting period. 	<ul style="list-style-type: none"> — Nonpublic companies are required to disclose transfers into and out of Level 3 assets and liabilities, as well as purchases and issues of Level 3 assets and liabilities instead of providing a detailed roll-forward. — For investments in certain companies that calculate net asset value, disclosures are only required for the timing of liquidation of an investee's assets, and the date when restrictions from redemption might lapse, if the investee has communicated the timing to the investor or has publicly announced it. — The measurement uncertainty disclosure communicates information about the uncertainty as of the reporting date. — Removed the term "at a minimum" from the disclosure requirements. 	<ul style="list-style-type: none"> — Changes in unrealized gains and losses for the period included in other comprehensive income. — The range and weighted average of significant observable inputs used. Alternatively, an entity may choose to disclose other quantitative information if it determines that is a more reasonable and rational method that reflects the distribution of unobservable inputs used.

The new guidance is effective for all entities for annual and interim periods in fiscal years beginning after December 15, 2019. Early adoption is allowed for any period for which financial statements have not yet been issued or made available for issuance. An entity is permitted to early adopt any eliminated or modified disclosure requirement and delay adoption of the additional disclosure requirements until their effective date.

Implementation costs of cloud computing arrangements

In August 2018, the FASB issued new guidance¹⁴ that requires implementation costs incurred by customers in cloud computing arrangements to be deferred and recognized over the term of the arrangement, if those costs would be capitalized by the customer in a software licensing arrangement under the internal-use software guidance in ASC 350–40. The arrangements under the scope of the guidance are "hosting arrangements" that do not transfer a software license to the customer.

Hosting arrangements are those that allow customers to access and use software on an as-needed basis without having possession of it.

The guidance requires companies to defer potentially significant, specified implementation costs incurred in a cloud computing arrangement that are often expensed as incurred under the current U.S. GAAP and recognize them to expense over the noncancellable term of the arrangement. The new deferred implementation cost assets will affect companies' financial ratios and deferred tax accounting.

The new guidance is effective for public companies for annual and interim reporting periods for fiscal years beginning after December 15, 2019. For all other companies, the guidance is effective for annual reporting periods for fiscal years beginning after December 15, 2020, and for interim reporting periods for fiscal years beginning after December 15, 2021. Early adoption is permitted.

¹⁴ FASB Accounting Standards Update No. 2018-15, *Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That is a Service Contract*



4 Proposed guidance

Recognizing an assumed liability in a revenue contract

The Emerging Issues Task Force (EITF) reached a consensus-for-exposure at its June 2018 meeting that would align the criteria for recognizing a liability for a revenue contract acquired in a business combination with the criteria for identifying a performance obligation in the revenue recognition standard. The EITF expects to issue an exposure draft in the fourth quarter.

Simplifying balance sheet debt classification

In August 2018, the Financial Accounting Standards Board (FASB) redeliberated its proposed ASU on simplifying the balance sheet classification of debt and tentatively decided these issues:

- *Unused long-term financing arrangement.* A borrower would disregard an unused long-term financing arrangement in place at the balance sheet date when determining the classification of debt unless it is explicitly available to refinance an existing debt. The FASB had previously decided that an existing unused long-term financing arrangement could support noncurrent presentation for current maturities of other debt arrangements.
- *Grace periods.* A borrower who violates a covenant for which there is a specified grace period to cure the violation would classify the debt as noncurrent. The borrower also would disclose the violation and information related to the grace period.

The new guidance would be effective for public companies for fiscal years and interim periods within those fiscal years beginning after December 15, 2020, and for all other entities for fiscal years beginning after December 15, 2021 and interim periods within fiscal years beginning after December 15, 2022.



5 Regulatory update

SEC amends investment company liquidity disclosures

An SEC final rule required registered investment companies to disclose in their reports to shareholders information about the operation and effectiveness of their liquidity risk management programs. The rule also rescinds and amends the requirement in Form N-PORT under the Investment Company Act of 1940.

SEC updates smaller reporting company (SRC) definition

Under an SEC final rule, registrants can qualify as an SRC if they have public float of less than \$250 million or annual revenues less than \$100 million as of their most recent fiscal year and either no public float or a public float of less than \$700 million. However, companies with more than \$75 million in public float will continue to be accelerated filers. The new definition allows more registrants to take advantage of scaled disclosures.

The final rule also amends Rule 3-05(b)(2)(iv) of Regulation S-X to increase from \$50 million to \$100 million the net revenue threshold for requiring three years of audited financial statements for an acquired business. Registrants may omit the financial statements of the acquired, or to be acquired, business for the earliest of the three fiscal years if net revenue reported by the acquired business in the most recent financial year are less than \$100 million.

SEC updates guidance on cybersecurity disclosures

In February 2018, the SEC commissioners approved new guidance¹⁵ which reinforces guidance issued by the Division of Corporate Finance in 2011. The new guidance reinforces existing disclosure requirements related to cybersecurity breaches and adds topics for consideration, including the required disclosure of material information, timeliness of disclosures, disclosure controls and procedures, and risk factors. The SEC issued this guidance in response to the increasing significance of cybersecurity incidents.

Even though the new guidance does not modify or create new SEC rules or regulations, it discusses how companies, both domestic and foreign, might consider cybersecurity matters when preparing disclosures in periodic SEC reports and registration statements. The new guidance does not apply to registered investment companies, registered investment advisers, brokers, dealers, and self-regulatory organizations. For those entities, other cybersecurity guidance¹⁶ exists. The new guidance is effective upon issuance.

SEC amends Investment Advisers Act

In March 2018, the SEC issued a final rule that amends certain investment adviser registration exemptions under the Investment Advisers Act of 1940 to reflect changes made by the Fixing America's Surface Transportation Act of 2015. Specifically, the final rule amends the definition of a "venture capital fund" to include small business investment companies, and the definition of "assets under management" to exclude the assets of small business investment companies. The rule became effective March 12, 2018.

SEC required interim disclosure of changes in stockholders' equity

Under a final rule issued by the SEC in August 2018, registrants will be required to disclose in interim periods on Form 10-Q the changes in each caption of stockholders' equity and noncontrolling interests for the current and comparative year-to-date periods, with subtotals for each interim period, and the amount of dividends per share for each class of shares. The amendments require registrants, including SRCs, to provide information as prescribed by Rule 3-04 of Regulation S-X. Accordingly, the interim disclosures of changes in stockholders' equity, including dividends per share amounts, may be given in a note to the financial statements or in a separate financial statement.

15 Commission Statement and Guidance on Public Company Cybersecurity Disclosures, Release Nos. 33-10459; 34-82746, February 21, 2018

16 Regulation Systems Compliance and Integrity. Release No. 34-73639, Nov. 19, 2014, and IM Guidance Update, No. 2015-02, April 2015



6 Appendix

Accounting standards affecting public companies in 2018

Calendar year-end public companies are required to begin applying these accounting standards in 2018.

Topic	Effective date for public companies	For more information
Revenue recognition	Annual and interim periods in fiscal years beginning after 12/15/2017	ASU 2014–09 ASU 2015–14 ASU 2016–08 ASU 2016–10 ASU 2016–11 ASU 2016–12 ASU 2016–20 ASU 2017–13 ASU 2017–14 KPMG’s webpage on Revenue
Recognition and measurement of financial assets and financial liabilities	Annual and interim periods in fiscal years beginning after 12/15/2017	ASU 2016–01 ASU 2018–04 KPMG’s webpage on Financial instruments
Technical corrections and improvements to financial instruments—Overall, Recognition and measurement of financial assets and financial liabilities	Fiscal years beginning after 12/15/2017, and interim periods in fiscal years beginning after 6/15/2018. Public business entities with fiscal years beginning in the period between 12/15/17 and 6/15/18 are not required to adopt the amendments until the interim period beginning after 6/15/18.	ASU 2018–03 KPMG’s webpage on Financial instruments
Recognition of breakage for certain prepaid stored-value products	Annual and interim periods in fiscal years beginning after 12/15/2017	ASU 2016–04 Defining Issues Podcast
Statement of cash flows—classification of certain cash receipts and payments	Annual and interim periods in fiscal years beginning after 12/15/2017	ASU 2016–15 Defining Issues Webcast Podcast
Intra-entity transfers of assets other than inventory	Annual and interim periods in fiscal years beginning after 12/15/2017	ASU 2016–16 Defining Issues Podcast
Statement of cash flows—presentation of restricted cash	Annual and interim periods in fiscal years beginning after 12/15/2017	ASU 2016–18 Defining Issues Webcast Podcast

Topic	Effective date for public companies	For more information
Clarifying the definition of a business	Annual and interim periods in fiscal years beginning after 12/15/2017	ASU 2017–01 Defining Issues Webcast
Clarifying the scope of asset derecognition guidance and accounting for partial sales of nonfinancial assets	Annual and interim periods in fiscal years beginning after 12/15/2017	ASU 2017–05 Defining Issues Podcast
Improving the presentation of net periodic pension cost and net periodic postretirement benefit cost	Annual and interim periods in fiscal years beginning after 12/15/2017	ASU 2017–07 Defining Issues Podcast
Scope of modification accounting for share-based payment awards	Annual and interim periods in fiscal years beginning after 12/15/2017	ASU 2017–09 Web article
Identifying the customer in a service concession arrangement	Annual and interim periods in fiscal years beginning after 12/15/2017	ASU 2017–10 Web article Podcast
Income Taxes (ASC 740): Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118	Effective upon issuance (March 2018)	ASU 2018–05
Codification Improvements to ASC 942, Financial Services—Depository and Lending	Effective upon issuance (May 2018)	ASU 2018–06 Web article
Not-For-Profit Entities (ASC 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made	Contributions received: Annual and interim periods in fiscal years beginning after 6/15/2018 Contributions made: Annual and interim periods in fiscal years beginning after 12/15/2018	ASU 2018–08 Defining Issues
Codification Improvements	Most amendments are effective upon issuance (July 2018). Certain amendments that require transition guidance are effective for fiscal years, and interim periods within those years, beginning after 12/15/2018. Other amendments, which affect recently issued ASUs that are not yet effective, are effective at the same time as the original ASU.	ASU 2018–09 Web article

Accounting standards affecting public companies in 2019 and beyond

Calendar year-end public companies are required to begin applying these accounting standards in 2019 or later and may need to disclose their potential effects in 2018.

Topic	Effective date for public companies	For more information
Leases	Annual and interim periods in fiscal years beginning after 12/15/2018	ASU 2016-02 ASU 2017-13 ASU 2018-01 ASU 2018-10 ASU 2018-11 KPMG's webpage on Leases
(Part I) Accounting for certain financial instruments with down round features, (Part II) Replacement of the indefinite deferral for mandatorily redeemable financial instruments of certain nonpublic entities and certain mandatorily redeemable noncontrolling interests with a scope exception	Annual and interim periods in fiscal years beginning after 12/15/2018	ASU 2017-11 Defining Issues
Targeted improvements to accounting for hedging activities	Annual and interim periods in fiscal years beginning after 12/15/2018	ASU 2017-12 Defining Issues
Codification improvements ASC 955, US Steamship Entities	Annual and interim periods in fiscal years beginning after 12/15/2018	ASU 2017-15 Web article
Reclassification of certain tax effects from accumulated other comprehensive income	Annual and interim periods in fiscal years beginning after 12/15/2018	ASU 2018-02 Tax reform supplement Webcast
Measurement of credit losses on financial instruments	<p>SEC filers: Annual and interim periods in fiscal years beginning after 12/15/2019</p> <p>Non-SEC filers: Annual and interim periods in fiscal years beginning after 12/15/2020</p>	ASU 2016-13 Defining Issues KPMG's webpage on Financial instruments

Topic	Effective date for public companies	For more information
Premium amortization for purchased callable debt securities	Annual and interim periods in fiscal years beginning after 12/15/2018	ASU 2017–08 Defining Issues Podcast
Compensation—Stock Compensation (ASC 718): Improvements to Nonemployee Share-Based Payment Accounting	Annual and interim periods in fiscal years beginning after 12/15/2018	ASU 2018–07 Defining Issues
Simplifying the test for goodwill impairment	SEC filers: Annual and interim periods in fiscal years beginning after 12/15/2019 Non-SEC filers: Annual and interim periods in fiscal years beginning after 12/15/2020	ASU 2017–04 Defining Issues Podcast
Financial Services—Insurance (ASC 944)	Annual and interim periods in fiscal years beginning after 12/15/2020	ASU 2018–12 Defining Issues
Fair Value Measurement (ASC 820)	Annual and interim periods in fiscal years beginning after 12/15/2019	ASU 2018–13 Defining Issues
Compensation—Retirement Benefits—Defined Benefit Plans (ASC 715–20)	Annual and interim periods in fiscal years ending after 12/15/2020	ASU 2018–14 Defining Issues
Intangibles—Goodwill and Other—Internal-Use Software (ASC 350–40)	Annual and interim periods in fiscal years beginning after 12/15/2019	ASU 2018–15 Defining Issues

Accounting standards affecting private companies in 2018

Calendar year-end private companies are required to begin applying these accounting standards in 2018.

Topic	Effective date for private companies	For more information
Technical corrections (December 2016)	Most amendments were effective on issuance (December 2016). Certain amendments that require transition guidance are effective for: <ul style="list-style-type: none"> — annual and interim periods in fiscal years beginning after 12/15/2016 (for fair value measurements); and — annual periods in fiscal years beginning after 12/15/2017, and interim periods in fiscal years beginning after 12/15/2018 (for cloud computing arrangements). 	ASU 2016–19
Scope of modification accounting for share-based payment awards	Annual and interim periods in fiscal years beginning after 12/15/2017	ASU 2017–09 Web article
Simplifying the presentation of deferred taxes	Annual periods in fiscal years beginning after 12/15/2017, and interim periods in fiscal years beginning after 12/15/2018	ASU 2015–17 Defining Issues Podcast
Effect of derivative contract novations on existing hedge accounting relationships	Annual periods in fiscal years beginning after 12/15/2017, and interim periods in fiscal years beginning after 12/15/2018	ASU 2016–05 Defining Issues Podcast
Contingent put and call options in debt instruments	Annual periods in fiscal years beginning after 12/15/2017, and interim periods in fiscal years beginning after 12/15/2018	ASU 2016–06 Defining Issues Podcast
Improvements to employee share-based payment accounting	Annual periods in fiscal years beginning after 12/15/2017, and interim periods in fiscal years beginning after 12/15/2018	ASU 2016–09 Defining Issues Podcast
Presentation of financial statements of not-for-profit entities	Annual periods in fiscal years beginning after 12/15/2017, and interim periods in fiscal years beginning after 12/15/2018	ASU 2016–14

Topic	Effective date for private companies	For more information
Income Taxes (ASC 740): Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118	Effective upon issuance (March 2018)	ASU 2018–05
Codification Improvements to ASC 942, Financial Services— Depository and Lending	Effective upon issuance (May 2018)	ASU 2018–06 Web article
Codification Improvements	Most amendments are effective upon issuance (July 2018). Certain amendments that require transition guidance are effective for fiscal years, and interim periods within those years, beginning after 12/15/2019. Other amendments, which affect recently issued ASUs that are not yet effective, are effective at the same time as the original ASU.	ASU 2018–09 Web article

Accounting standards affecting private companies in 2019 and beyond

Calendar year-end private companies are required to begin applying these accounting standards in 2019 or later.

Topic	Effective date for private companies	For more information
Codification improvements to ASC 955, US Steamship Entities	Annual and interim periods in fiscal years beginning after 12/15/2018	ASU 2017–15 Web article
Reclassification of certain tax effects from accumulated other comprehensive income	Annual and interim periods in fiscal years beginning after 12/15/2018	ASU 2018–02 Tax reform supplement Webcast
Revenue recognition	Annual periods in fiscal years beginning after 12/15/2018, and interim periods in fiscal years beginning after 12/15/2019	ASU 2014–09 ASU 2015–14 ASU 2016–08 ASU 2016–10 ASU 2016–12 ASU 2016–20 KPMG’s webpage on Revenue
Recognition and measurement of financial assets and financial liabilities	Annual periods in fiscal years beginning after 12/15/2018, and interim periods in fiscal years beginning after 12/15/2019	ASU 2016–01 ASU 2018–03 ASU 2018–04 KPMG’s webpage on Financial instruments
Recognition of breakage for certain prepaid stored-value products	Annual periods in fiscal years beginning after 12/15/2018, and interim periods in fiscal years beginning after 12/15/2019	ASU 2016–04 Defining Issues Podcast
Statement of cash flows—classification of certain cash receipts and payments	Annual periods in fiscal years beginning after 12/15/2018, and interim periods in fiscal years beginning after 12/15/2019	ASU 2016–15 Defining Issues Webcast Podcast
Intra-entity transfers of assets other than inventory	Annual periods in fiscal years beginning after 12/15/2018, and interim periods in fiscal years beginning after 12/15/2019	ASU 2016–16 Defining Issues Podcast
Statement of cash flows—presentation of restricted cash	Annual periods in fiscal years beginning after 12/15/2018, and interim periods in fiscal years beginning after 12/15/2019	ASU 2016–18 Defining Issues Webcast Podcast

Topic	Effective date for private companies	For more information
Clarifying the definition of a business	Annual periods in fiscal years beginning after 12/15/2018, and interim periods in fiscal years beginning after 12/15/2019	ASU 2017-01 Defining Issues Webcast
Clarifying the scope of asset derecognition guidance and accounting for partial sales of nonfinancial assets	Annual periods in fiscal years beginning after 12/15/2018, and interim periods in fiscal years beginning after 12/15/2019	ASU 2017-05 Defining Issues Podcast
Employee benefit plan master trust reporting	Annual periods in fiscal years beginning after 12/15/2018	ASU 2017-06 Web article
Improving the presentation of net periodic pension cost and net periodic postretirement benefit cost	Annual periods in fiscal years beginning after 12/15/2018, and interim periods in fiscal years beginning after 12/15/2019	ASU 2017-07 Defining Issues Podcast
Identifying the customer in a service concession arrangement	Annual periods in fiscal years beginning after 12/15/2018, and interim periods in fiscal years beginning after 12/15/2019	ASU 2017-10 Web article Podcast
Not-For-Profit Entities (ASC 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made	<p>Contributions received: Annual periods in fiscal years beginning after 12/15/2018, and interim periods in fiscal years beginning after 12/15/2019</p> <p>Contributions made: Annual periods in fiscal years beginning after 12/15/2019, and interim periods in fiscal years beginning after 12/15/2020</p>	ASU 2018-08 Defining Issues
Leases	Annual periods in fiscal years beginning after 12/15/2019, and interim periods in fiscal years beginning after 12/15/2020	ASU 2016-02 ASU 2018-01 ASU 2018-10 ASU 2018-11 KPMG's webpage on Leases
Premium amortization for purchased callable debt securities	Annual periods in fiscal years beginning after 12/15/2019, and interim periods in fiscal years beginning after 12/15/2020	ASU 2017-08 Defining Issues Podcast

Topic	Effective date for private companies	For more information
(Part I) Accounting for certain financial instruments with down round features, (Part II) Replacement of the indefinite deferral for mandatorily redeemable financial instruments of certain nonpublic entities and certain mandatorily redeemable noncontrolling interests with a scope exception	Annual periods in fiscal years beginning after 12/15/2019, and interim periods in fiscal years beginning after 12/15/2020	ASU 2017–11 Defining Issues
Targeted improvements to accounting for hedging activities	Annual periods in fiscal years beginning after 12/15/2019, and interim periods in fiscal years beginning after 12/15/2020	ASU 2017–12 Defining Issues
Compensation—Stock Compensation (ASC 718): Improvements to Nonemployee Share-Based Payment Accounting	Annual periods in fiscal years beginning after 12/15/2019, and interim periods in fiscal years beginning after 12/15/2020	ASU 2018–07 Defining Issues
Measurement of credit losses on financial instruments	Annual periods in fiscal years beginning after 12/15/2020, and interim periods in fiscal years beginning after 12/15/2021	ASU 2016–13 Defining Issues KPMG’s webpage on Financial instruments
Simplifying the test for goodwill impairment	Annual and interim periods in fiscal years beginning after 12/15/2021	ASU 2017–04 Defining Issues Podcast
Financial Services—Insurance (ASC 944)	Annual periods in fiscal years beginning after 12/15/2021, and interim periods in fiscal years beginning after 12/15/2022	ASU 2018–12 Defining Issues
Fair Value Measurement (ASC 820)	Annual and interim periods in fiscal years beginning after 12/15/2019	ASU 2018–13 Defining Issues
Compensation—Retirement Benefits—Defined Benefit Plans (ASC 715–20)	Annual and interim periods in fiscal years ending after 12/15/2021	ASU 2018–14 Defining Issues
Intangibles—Goodwill and Other—Internal-Use Software (ASC 350–40)	Annual periods in fiscal years beginning after 12/15/2020, and interim periods in fiscal years beginning after 12/15/2021	ASU 2018–15 Defining Issues



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