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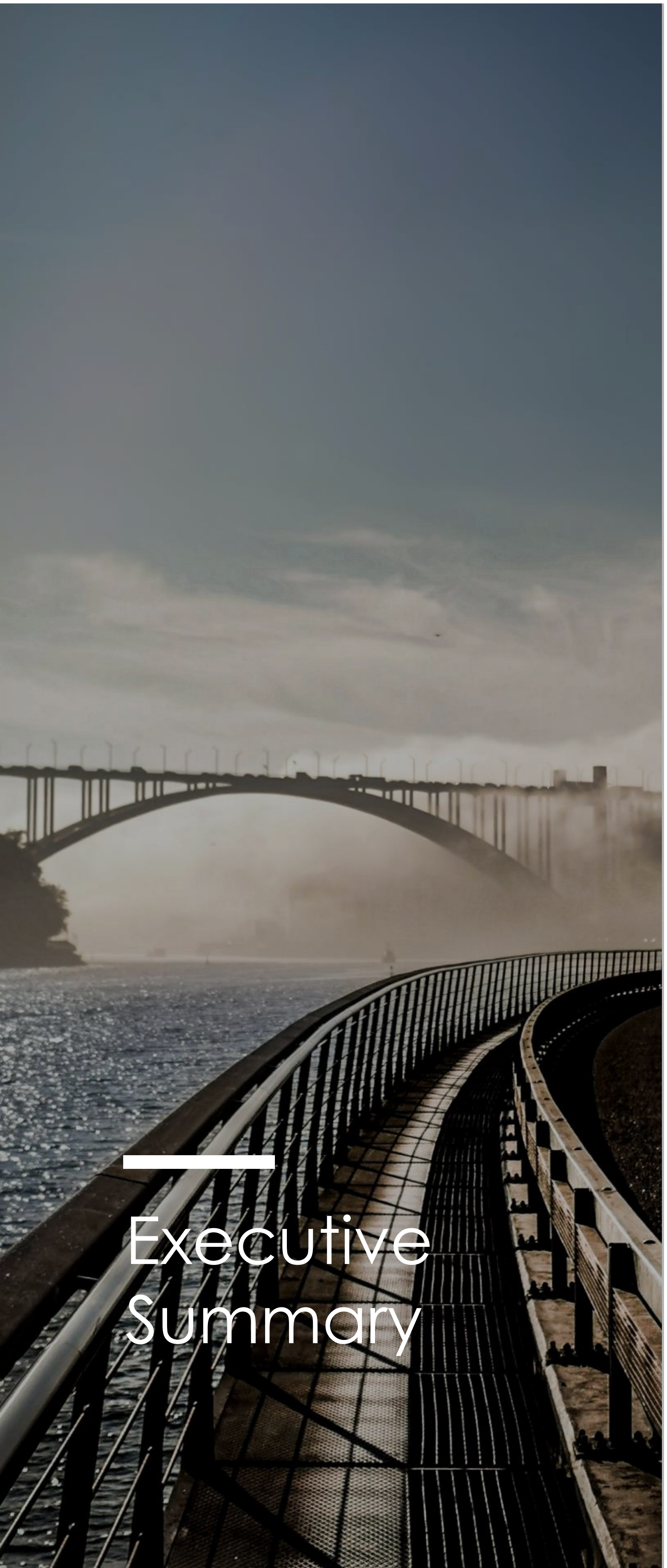
INDUSTRY INSIGHTS

Q2 2024 // PREPARED BY CNM PROFESSIONAL PRACTICE GROUP



Executive Summary

Q2 2024

Key Insights

Dear Colleagues and Friends,

In this issue of Industry Insights, we discuss the latest accounting and financial reporting developments for the second quarter of 2024.

In our Accounting and Financial Reporting update section, we discuss SEC comment letter trends. We note that the traditional topics such as Non-GAAP measures, MD&A and revenue recognition continue to generate the highest number of comments in recent years. In addition to the traditional topics, the SEC is focused on the disclosures surrounding the current hot topics such as inflation and interest rates, supply chain, Ukraine/China/Israel, and impairment considerations amongst other topics. The SEC encourages registrants to revisit the risk factors disclosure in the MD&A and address why certain things pose a risk and how the company will be remediating that risk.

In our SEC updates section, we also provide a summary of a recent statement published by Corp. Fin. on nuances of cybersecurity disclosure rule and the SEC's expectation from registrants on assessing materiality and determining the appropriate 8-K filing.

In our FASB update section, we discuss three major projects that are currently on the agenda: the software costs project, the disaggregation of income statement expenses, and Induced conversion of convertible debt instruments. There are recent updates on all three projects and the Board expects to have either a final ASU or an exposure draft issued on them by the end of the year.

Q2 2024

SEC Clarification on material vs. non-material cyber incidents

In May, the Division of Corporation Finance released a statement to clarify the content that should be included on the Form 8-K for cybersecurity incidents. The SEC rule, adopted in July 2023, requires companies to disclose material cybersecurity incidents on Item 1.05 (Material Cybersecurity Incidents) of Form 8-K. If, however, companies have cybersecurity incidents that are not material, or the company has not made the materiality assessment at the time of filing, the SEC encourages the voluntary disclosure of these events under Item 8.01 (Other Events) instead of Item 1.05. The SEC clarified that if within 4 business days, the company has not determined materiality impact of the cybersecurity incident, a registrant is encouraged to file an 8K Form and report the incident under Item 8.01. Once materiality is determined and if the incident is deemed to be material, a second 8K Form should be filed to include the details of the incident under Item 1.05. The SEC also encourages companies to have a process in place and a dedicated team who can perform the material assessment of such incidents within a few days of the incident.

SEC Comment Letter Trends

During the recent years, we have noted that the traditional topics with the highest number of comments continue to be the non-GAAP measures, MD&A, revenue recognition, business combinations and segment reporting. The SEC emphasized the importance of revisiting the year over year disclosures, and refrain from boilerplate disclosures. They encouraged registrants to think about the “why” when they prepare the disclosures and make them tailored for their investors and other users of the financial statements.

In addition to the traditional list with high number of comment letters, there are a number of hot topics that are on the staff’s radar, including inflation and interest rates, supply chain, Ukraine/China/Israel, Impairment and Climate-related disclosures. Registrants are encouraged to be specific and tailored when including disclosures within the MD&A and as part of the risk factors.

Additionally, the staff has been focused on registrants’ cybersecurity disclosures including on the Form 10-K and 8-K. The comment letters generally ask for additional information on the type of incident and its impact.

FASB expects an exposure draft on disclosure of software costs in Q3 2024

The FASB directed the staff to draft a proposed ASU on Accounting for and Disclosure of software costs at its June 18th meeting. The Board expects to have an exposure draft out to public within the next few months.

In this project, the Board has decided to pursue targeted improvements to the internal use software model and explore potential improvements to disclosures. The decision is driven by feedback received from the investors, who said that they are not looking for additional capitalizations on the balance sheet and could benefit from more transparency on the expenses spent on software.

FASB to draft a final ASU on the Disaggregation of Income Statement Expenses

As a reminder to our readers, the disaggregation of income statement (DISE) project, was put on the agenda because feedback from investors, lenders and other users of financial statements indicated that more detailed information about expenses is critically important in understanding an entity's performance. The proposed ASU included the following 4 categories of footnote disclosures:

1. Disaggregation of each expense line item based on the following categories:
    a. inventory and manufacturing expense,
    b. employee compensation,
    c. depreciation, and
    d. amortization of intangibles.
2. Disaggregation of Inventory and Manufacturing expense into:
    a. purchases of inventory
    b. employee compensation
    c. depreciation
    d. amortization of intangibles, and other cost of products sold, as applicable (i.e. warranty expense, freight, etc. to be defined by the entity in an annual disclosure).
3. Disclose qualitatively descriptions of amounts remaining in relative expense captions that are not separately disaggregated quantitatively.
4. Disclose total "selling expenses" and annually, the company's definition of "selling expenses."

During the June 18th meeting, the Board has made the following tentative decisions:

1. The Board decided not to provide a practical expedient that would allow an entity to combine costs of product revenue and cost of service revenue into one expense caption.
2. Pursue a single disaggregation approach that would
    a. remove inventory and manufacturing expense as a required category, and
    b. add purchase of inventory as a required category.

FASB to Issue a Final ASU on Induced Conversion of Convertible Debt Instruments

In November 2022, this agenda request was submitted to the Board requesting that the Emerging Task Force (EITF) address whether certain convertible debt instruments settled using terms that differ from their stated contractual conversion provisions should be accounted for as an induced conversion or an extinguishment.

The Task Force reached a consensus-for-exposure to:

1. Pursue the preexisting contract approach for induced conversion assessment. Under this approach, only conversions that include the issuance of all the consideration (in form and amount) pursuant to conversion privileges included in the terms of the debt at issuance would be accounted for as induced conversions.
2. When evaluating whether the amount of cash (or combination of cash and shares) issuable under the original conversion privileges is preserved by the inducement offer.
3. An entity should determine the amount of cash and number of shares that would be issued based on the fair value of the entity's shares as of the offer acceptance date.
4. If within a year leading up to the offer acceptance date the debt has been exchanged or modified without being deemed to be substantially different, then the debt terms that existed a year ago should be used in place of the terms of the debt at issuance.
5. Apply induced conversion accounting to all convertible debt instruments, including instruments that are not currently convertible, so long as those instruments contained a substantive conversion feature as of the time of issuance and are within the scope of the guidance in Subtopic 470-20, Debt—Debt with Conversion and Other Options.

The Board expects a final ASU issued on this topic during Q3 2024.

FASB Technical Agenda* as of June 26, 2024

FASB Milestone	Project
RESEARCH PROJECTS	Accounting for and Disclosure of Intangibles Accounting for Commodities Agenda Consultation Consolidation for Business Entities Definition of a Derivative Financial key performance Indicators for Business Entities Statement of Cash Flows
BOARD DELIBERATION	Accounting for and Disclosure of Software Costs Accounting for Environmental Credit Program Accounting for Government Grants Codification Improvements (next Phase) Statement of Cash Flows Targeted Improvements
EXPOSURE DRAFT	Topic 815 - Derivative Scope Refinements Topic 815 - Hedge Accounting Improvements Interim Reporting - Narrow Scope Improvements- Expected Q3 2024
BOARD REDELIBERATION	Financial Instruments - Credit Losses (Topic 326)- Purchased Financial Assets Disaggregation: Income Statement Expenses
EXPECTED FINAL ASU	Induced Conversions of Convertible Debt Instruments (EITF No. 23-A) - Expected Q3 2024
FINAL ASU	ASU 2024-01- Compensation - Stock Compensation (Topic 718): Scope Application of Profit Interest and Similar Awards ASU 2024-02 - Codification Improvements - Amendments to Remove References to the Concepts Statements

* https://www.fasb.org/technicalagenda

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Who is CNM?

Founded in 2003, CNM LLP is recognized as one of the premier technical advisory firms in Southern California with Big 4 experience that provides the responsive customer service of a boutique firm. And we're a dynamic team that enlists all our energy to help transform the way your company does business – carefully evaluating your needs, simplifying your financial processes, and passionately solving problems in the most cost-effective way.

Our extensive knowledge of US GAAP, ICFR and SEC reporting skills has given us the ability to assist our clients with transactions that are not only multifaceted, but the capability to implement new or complex accounting standards. We have over 200 global professionals in our Los Angeles, Orange County, San Diego, New York City, and Kuala Lumpur offices. Many of our clients are developed from direct referrals from the Big 4 accounting firms, speaking to the level of quality services we provide.

To learn more about how we can help, visit our website at www.cnmllp.com.

CNM LLP
Technical Advisory Firm

Los Angeles

A | 6320 Canoga Avenue
Suite 150
Woodland Hills, CA 91367
O | 818.999.9501

Orange County

A | 15635 Alton Parkway
Suite 450
Irvine, CA 92618
O | 949.299.5582

San Diego

A | 12671 High Bluff Drive
Suite 350
San Diego, CA 92130

New York City

A | 264 West 40th Street
19th Floor
New York, NY 10018

Malaysia

A | Suite 19-01, GTower,
199, Jalan Tun Razak,
50400 Kuala Lumpur