Accounting Rule Changes with Minimal (or no) Impact on Models – December 2021

This report gives investors the scoop on what's happening at the Financial Accounting Standards Board (FASB) and International Accounting Standards Board (IASB) and how newly issued accounting standards updates (ASUs) affect fundamental research.

Each of the below ASUs will affect how companies report financial information, but they have minimal or no impact on our financial models. Get more details on other recent ASUs, and their impact on our models, here.

ASU 2021-07 – Compensation – Stock Compensation (Topic 718) Determining the Current Price of an Underlying Share for Equity-Classified Share-Based Awards

This update allows a nonpublic entity to determine the current price input of equity-classified share-based awards issued to both employees and nonemployees using the reasonable application of a reasonable valuation method. Characteristics of the reasonable application of a reasonable valuation method include:

1. Date on which a valuation's reasonableness is evaluated
2. Factors that a reasonable valuation should consider
3. Scope of information that a reasonable valuation should consider
4. Criteria that should be met for the use of a previously calculated value to be considered reasonable

The amendments in this update are effective for fiscal years beginning after December 15, 2021 and create no changes to our models.

ASU 2021-08 – Business Combinations (Topic 805): Accounting for Contract Assets and Contract Liabilities from Contracts with Customers

This update requires an entity to recognize and measure contract assets and liabilities acquired in a business combination in accordance with a previous accounting standard (Topic 606). At the acquisition date, an acquirer should account for the revenue contracts as if it had originated the contracts. Generally, this update should result in an acquirer recognizing and measuring the acquired contract assets and contract liabilities consistent with how they were recognized and measured in the acquiree's financial statements.

Before this update, acquirers recognized these assets and liabilities at fair value during a business combination.

The amendments in this update improve the comparability by specifying for all acquired revenue contracts regardless of their timing of payment:

1. The circumstances in which the acquirer should recognize contract assets and contract liabilities that are acquired in a business combination and
2. How to measure those contract assets and liabilities

The amendments in this update are effective for fiscal years beginning after December 15, 2022. This update requires no changes to our models.

ASU 2021-09 – Leases (Topic 842): Discount Rate for Leases That are Not Public Business Entities

This update affects lessees that are not public business entities, including not-for-profit entities. These entities can now elect as an accounting policy to use a risk-free rate as the discount rate for all leases. Lessees can now make the risk-free rate election by class of underlying asset, rather than at the entity-wide level. The entity will also be required to disclose which asset classes it has elected to apply a risk-free rate.

This amendment also requires that when the rate implicit in the lease is readily determinable for any individual lease, the lessee uses that rate rather than making a risk-free rate election.

The amendments in this update are effective after December 15, 2022. This update requires no changes to our models.

ASU 2021-10 – Government Assistance (Topic 832): Disclosures by Business Entities about Government Assistance

This update increases the transparency of government assistance by requiring companies to disclose:

1. The types of assistance
2. An entity's accounting for the assistance
3. The effect of the assistance on the entity's financial statements

Currently, there is a lack of specific authoritative guidance regarding government assistance in GAAP. This update will greatly improve the transparency and comparability of information to financial statement users.

The amendments in this update are effective for all entities beginning December 15, 2021. This requires no changes to our models. We applaud FASB for increasing the transparency around these transactions.

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Disclosure: David Trainer, Kyle Guske II, and Matt Shuler receive no compensation to write about any specific stock, sector, style, or theme.

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1. Legacy fundamental datasets suffer from significant inaccuracies, omissions and biases.
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3. Our proprietary measures of Core Earnings and Earnings Distortion materially improve stock picking and forecasting of profits.

Best Fundamental Data in the World

Forthcoming in The Journal of Financial Economics, a top peer-reviewed journal, Core Earnings: New Data & Evidence proves our Robo-Analyst technology overcomes material shortcomings in legacy firms' data collection processes to provide superior fundamental data, earnings models, and research. More details.

Key quotes from the paper:

- "[New Constructs'] *Total Adjustments* differs significantly from the items identified and excluded from Compustat's adjusted earnings measures. For example… 50% to 70% of the variation in *Total Adjustments* is not explained by *S&P Global's (SPGI) Adjustments* individually." – pp. 14, 1st para.
- "A final source of differences [between New Constructs' and S&P Global's data] is due to data collection oversights…we identified cases where Compustat did not collect information relating to firms' income that is useful in assessing core earnings." – pp. 16, 2nd para.

Superior Models

A top accounting firm features the superiority of our ROIC, NOPAT and Invested Capital research to Capital IQ & Bloomberg's in Getting ROIC Right. See the Appendix for direct comparison details.

Key quotes from the paper:

- "…an accurate calculation of ROIC requires more diligence than often occurs in some of the common, off-the-shelf ROIC calculations. Only by scouring the footnotes and the MD&A [as New Constructs does] can investors get an accurate calculation of ROIC." – pp. 8, 5th para.
- "The majority of the difference…comes from New Constructs' machine learning approach, which leverages technology to calculate ROIC by applying accounting adjustments that may be buried deeply in the footnotes across thousands of companies." – pp. 4, 2nd para.

Superior Stock Ratings

Robo-Analysts' stock ratings outperform those from human analysts as shown in this paper from Indiana's Kelley School of Business. Bloomberg features the paper here.

Key quotes from the paper:

- "the portfolios formed following the buy recommendations of Robo-Analysts earn abnormal returns that are statistically and economically significant." – pp. 6, 3rd para.
- "Our results ultimately suggest that Robo-Analysts are a valuable, alternative information intermediary to traditional sell-side analysts." – pp. 20, 3rd para.

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